

NEW ISSUE
BOOK-ENTRY ONLY

RATINGS:
Moody's: "Aaa"
S&P: "AAA"
Fitch: "AAA"
(See "RATINGS" and
"BOND INSURANCE" herein.)

In the opinion of Bond Counsel, McCall, Parkhurst & Horton L.L.P., assuming continuing compliance by the City of San Antonio, Texas, after the date of issuance of the Bonds (defined below) with certain covenants in the Ordinance described herein and subject to the matters discussed herein under "TAX MATTERS," interest on the Bonds is excludable from gross income for federal income tax purposes under existing statutes, published rulings, regulations, and court decisions and will be an item of tax preference for the purpose of determining the alternative minimum tax imposed on individuals and corporations. For further information, see "TAX MATTERS" herein.



\$17,850,000
CITY OF SAN ANTONIO, TEXAS AIRPORT SYSTEM
REVENUE REFUNDING BONDS, SERIES 2006
(Alternative Minimum Tax Bonds)



Date: November 1, 2006

Due: July 1, as shown herein

The \$17,850,000 "City of San Antonio, Texas Airport System Revenue Refunding Bonds, Series 2006" (the "Bonds") are being issued by the City of San Antonio, Texas (the "City") pursuant to the laws of the State of Texas, including Chapter 22, Texas Transportation Code; and Chapters 1207 and 1503, Texas Government Code; a master ordinance adopted by the City Council of the City (the "City Council") on April 19, 2001 (the "Master Ordinance"); and an Eighth Supplement to the Master Ordinance adopted by the City Council on November 16, 2006. (See "THE BONDS – Authority for Issuance" herein.)

Interest on the Bonds will accrue from November 1, 2006, will be payable January 1 and July 1 of each year (commencing July 1, 2007), and will be calculated on the basis of a 360-day year composed of twelve 30-day months. The Bonds will be issued as fully registered obligations in book-entry-only form and when issued will be registered in the name of Cede & Co., as nominee of The Depository Trust Company ("DTC"), New York, New York. DTC will act as securities depository (the "Securities Depository"). Book-entry interests in the Bonds will be made available for purchase in the principal amount of \$5,000 or any integral multiple thereof. Purchasers of the Bonds (the "Beneficial Owners") will not receive physical delivery of certificates representing their interest in the Bonds. So long as the Securities Depository is the registered owner of the Bonds, the principal of and interest on the Bonds will be payable by The Bank of New York Trust Company, National Association, Dallas, Texas, as the initial Paying Agent/Registrar, to the Securities Depository, which will in turn remit such principal and interest to its participants, which will in turn remit such principal and interest to the Beneficial Owners. (See "BOOK-ENTRY-ONLY SYSTEM" herein.)

The Bonds are not subject to redemption prior to the date of maturity thereof.

The Bonds are special obligations of the City payable solely from and equally and ratably secured by a first lien on and pledge of the Gross Revenues (defined herein) derived from its ownership and operation of the Airport System. No mortgage of or lien on any of the physical properties forming a part of the Airport System has been given to secure the payment of the Bonds. The Bonds are issued on parity with certain outstanding bonds of the City that are also payable from and secured by a first lien on and pledge of the Gross Revenues. Neither the taxing power of the City or the State of Texas (or any political subdivision thereof), nor any other funds of the City are pledged to the payment of the Bonds.

The scheduled payment of principal of and interest on the Bonds when due will be guaranteed under an insurance policy to be issued concurrently with the delivery of the Bonds by Financial Security Assurance Inc. (See "BOND INSURANCE" herein.)



SEE INSIDE COVER PAGE FOR STATED MATURITIES, PRINCIPAL AMOUNTS, INTEREST RATES,
INITIAL YIELDS, CUSIP NUMBERS, AND REDEMPTION PROVISIONS FOR THE BONDS

The Bonds are offered for delivery, when, as, and if issued and received by the initial purchasers thereof named below (collectively, the "Underwriters") and are subject to the approving opinion of the Attorney General of the State of Texas and the legal opinion of McCall, Parkhurst & Horton L.L.P., San Antonio, Texas, Bond Counsel. (See "LEGAL MATTERS" herein.) Certain legal matters will be passed upon for the City by the City Attorney, and for the Underwriters by their counsel, Winstead Sechrest & Minick P.C., San Antonio, Texas. The Bonds are expected to be available for delivery through the services of DTC on or about December 13, 2006.

SIEBERT BRANDFORD SHANK & CO., LLC

PIPER JAFFRAY & CO.

UBS INVESTMENT BANK

STATED MATURITIES, PRINCIPAL AMOUNTS, INTEREST RATES, INITIAL YIELDS, AND INITIAL CUSIP NUMBERS

\$17,850,000
CITY OF SAN ANTONIO, TEXAS
AIRPORT SYSTEM REVENUE REFUNDING BONDS, SERIES 2006
(Alternative Minimum Tax Bonds)

<u>Maturity</u> <u>(July 1)</u>	<u>Principal</u> <u>Amount</u>	<u>Interest</u> <u>Rate</u>	<u>Initial</u> <u>Yield</u>	<u>Initial CUSIP</u> <u>Number</u> ⁽¹⁾
2007	\$1,465,000	5.000%	3.660%	796242 MA 0
2008	1,125,000	5.000	3.710	796242 MB 8
2009	1,165,000	5.000	3.760	796242 MC 6
2010	2,410,000	5.000	3.800	796242 MD 4
2011	2,540,000	5.000	3.820	796242 ME 2
2012	2,645,000	5.000	3.860	796242 MF 9
2013	2,800,000	5.000	3.890	796242 MG 7
2014	3,700,000	5.000	3.930	796242 MH 5

The Bonds are not subject to redemption prior to the maturity thereof.

⁽¹⁾ CUSIP numbers have been assigned to the Bonds by Standard & Poor's CUSIP Service Bureau, A Division of The McGraw-Hill Companies, Inc., and are included solely for the convenience of the owners of the Bonds. Neither the City, the Co-Financial Advisors, nor the Underwriters are responsible for the selection or correctness of the CUSIP numbers set forth herein.

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CITY OF SAN ANTONIO, TEXAS

CITY COUNCIL

Name	Years on City Council	Term Expires	Occupation
Phil Hardberger, Mayor	1 Year, 4 Months	May 31, 2007	Retired Appellate Court Judge
Roger O. Flores, District 1	3 Years, 4 Months	May 31, 2007	Restaurant Owner
Sheila D. McNeil, District 2	1 Year, 4 Months	May 31, 2007	Self-Employed
Roland Gutierrez, District 3	1 Year, 4 Months	May 31, 2007	Attorney
Richard Perez, District 4	3 Years, 4 Months	May 31, 2007	Self-Employed
Patti Radle, District 5	3 Years, 4 Months	May 31, 2007	Agency Director and Teacher
Delicia Herrera, District 6	1 Year, 4 Months	May 31, 2007	Self-Employed
Elena Guajardo, District 7	1 Year, 4 Months	May 31, 2007	Retired
Art A. Hall, District 8	3 Years, 4 Months	May 31, 2007	Attorney, Investment Banker
Kevin Wolff, District 9	1 Year, 4 Months	May 31, 2007	President, Employment Recruiting Firm
Christopher "Chip" Haass, District 10	3 Years, 4 Months	May 31, 2007	Educator

CITY OFFICIALS

Name	Position	Years with City of San Antonio	Years in Current Position
Sheryl L. Sculley	City Manager	11 Months	11 Months
Jelynn L. Burley	Deputy City Manager	22 Years, 6 Months	8 Months
Pat DiGiovanni	Deputy City Manager	7 Months	7 Months
Michael Armstrong	Assistant City Manager/ Chief Information Officer	1 Year, 2 Months	1 Year, 2 Months
Frances A. Gonzalez	Assistant City Manager	22 Years	2 Years, 11 Months
Erik J. Walsh	Assistant City Manager	12 Years, 4 Months	8 Months
Penny Postoak Ferguson	Assistant City Manager	1 Month	1 Month
Michael D. Bernard	City Attorney	11 Months	11 Months
Leticia M. Vacek	City Clerk	2 Years, 4 Months	2 Years, 4 Months
Thomas G. Wendorf	Director of Public Works	7 Years, 6 Months	5 Years, 9 Months
Ben Gorzell	Director of Finance	15 Years, 11 Months	4 Months ⁽¹⁾
Peter Zanon	Director of Management and Budget	9 Years, 6 Months	2 Years, 9 Months
Mark Webb	Director of Aviation	11 Years, 6 Months	4 Months ⁽²⁾

⁽¹⁾ Appointed Director of Finance on June 12, 2006; previously served as Acting Director of Finance from January 10, 2006, until date of permanent appointment.

⁽²⁾ Appointed Director of Aviation on June 12, 2006; previously served as Interim Director of Aviation from November 21, 2005, until date of permanent appointment.

CONSULTANTS AND ADVISORS

Bond Counsel McCall, Parkhurst & Horton L.L.P., San Antonio, Texas

Co-Certified Public Accountants * KPMG L.L.P., San Antonio, Texas,
Leal & Carter, P.C., San Antonio, Texas,
and Robert J. Williams, CPA, San Antonio, Texas

Co-Financial Advisors Coastal Securities, San Antonio, Texas
and Estrada Hinojosa & Company, Inc., San Antonio, Texas

Airport Consultant Unison Maximus

* KPMG L.L.P., Leal & Carter, P.C., and Robert J. Williams, CPA, the City's independent auditors, have not been engaged to perform and have not performed, since the date of its report included herein, any procedures on the financial statements addressed in that report. KPMG L.L.P., Leal & Carter, P.C., and Robert J. Williams, CPA, also have not performed any procedures relating to this Official Statement.

USE OF INFORMATION IN THE OFFICIAL STATEMENT

This Official Statement and the information contained herein are subject to completion and amendment. Under no circumstances will this Official Statement constitute an offer to sell or the solicitation of an offer to buy, nor will there be any sale of these securities in any jurisdiction in which such offer, solicitation, or sale would be unlawful prior to registration or qualification under the securities laws of such jurisdiction.

No dealer, broker, salesman, or other person has been authorized by the City to give any information or to make any representation with respect to the Bonds, other than as contained in this Official Statement, and if given or made, such other information or representations must not be relied upon as having been authorized by either of the foregoing. The information set forth herein has been obtained from sources which are believed to be reliable but is not guaranteed as to accuracy or completeness and is not to be construed as a representation by the Co-Financial Advisors or the Underwriters. The information and expressions of opinion herein are subject to change without notice, and neither the delivery of this Official Statement nor any sale made hereunder will under any circumstances create any implication that there has been no change in the information or opinions set forth herein after the date of this Official Statement.

THE BONDS ARE EXEMPT FROM REGISTRATION WITH THE SECURITIES AND EXCHANGE COMMISSION (THE "SEC") AND CONSEQUENTLY HAVE NOT BEEN REGISTERED THEREWITH. THE REGISTRATION, QUALIFICATION, OR EXEMPTION OF THE BONDS IN ACCORDANCE WITH APPLICABLE SECURITIES LAW PROVISIONS OF THE JURISDICTIONS IN WHICH THESE SECURITIES HAVE BEEN REGISTERED, QUALIFIED, OR EXEMPTED SHOULD NOT BE REGARDED AS A RECOMMENDATION THEREOF.

All information contained in this Official Statement is subject, in all respects, to the complete body of information contained in the original sources thereof and no guaranty, warranty, or other representation is made concerning the accuracy or completeness of the information herein. In particular, no opinion or representation is rendered as to whether any projection will approximate actual results, and all opinions, estimates and assumptions, whether or not expressly identified as such, should not be considered statements of fact.

IN CONNECTION WITH THE OFFERING OF THE BONDS, THE UNDERWRITERS MAY OVERALLOT OR EFFECT TRANSACTIONS THAT STABILIZE OR MAINTAIN THE MARKET PRICE OF THE BONDS AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANYTIME.

The Underwriters have provided the following sentence for inclusion in this Official Statement. The Underwriters have reviewed the information in this Official Statement in accordance with, and as part of, their responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriters do not guarantee the accuracy or completeness of such information.

The Co-Financial Advisors have provided the following sentence for inclusion in this Official Statement. The Co-Financial Advisors have reviewed the information in this Official Statement in accordance with, and as part of, their responsibilities to the City and, as applicable, to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Co-Financial Advisors do not guarantee the accuracy or completeness of such information.

The agreements of the City and others related to the Bonds are contained solely in the contracts described herein. Neither this Official Statement nor any other statement made in connection with the offer or sale of the Bonds is to be construed as constituting an agreement with the purchasers of the Bonds. INVESTORS SHOULD READ THE ENTIRE OFFICIAL STATEMENT, INCLUDING ALL APPENDICES ATTACHED HERETO, TO OBTAIN INFORMATION ESSENTIAL TO MAKING AN INFORMED INVESTMENT DECISION.

Neither the City, the Co-Financial Advisors, nor the Underwriters make any representation or warranty with respect to the information contained in this Official Statement regarding The Depository Trust Company or its Book-Entry-Only System.

Other than with respect to information concerning Financial Security Assurance Inc. ("Financial Security") contained under the caption "BOND INSURANCE" herein and "SPECIMEN INSURANCE POLICY" attached hereto as Appendix F herein, none of the information in this Official Statement has been supplied or verified by Financial Security and Financial Security makes no representation or warranty, express or implied, as to (i) the accuracy or completeness of such information; (ii) the validity of the Bonds; or (iii) the tax-exempt status of the interest on the Bonds.

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OFFICIAL STATEMENT
Relating to the
\$17,850,000
CITY OF SAN ANTONIO, TEXAS AIRPORT SYSTEM
REVENUE REFUNDING BONDS, SERIES 2006
(Alternative Minimum Tax Bonds)

INTRODUCTION

This Official Statement of the City of San Antonio, Texas (the "City") provides certain information in connection with the sale by the City of its \$17,850,000 "City of San Antonio, Texas Airport System Revenue Refunding Bonds, Series 2006" (the "Bonds"). This Official Statement describes the Bonds, the Ordinance (defined herein), and certain other information about the City and its Airport System (defined herein). All descriptions of documents contained herein are only summaries and are qualified in their entirety by reference to each such document. Capitalized terms used, but not defined, herein have the respective meanings assigned thereto in the "EXCERPTS FROM ORDINANCE" attached hereto as Appendix B. Copies of transaction documents may be obtained from the City at the Office of the Director of Finance, City Hall Annex, 506 Dolorosa, San Antonio, Texas 78204 and, during the offering period, from the City's Co-Financial Advisors, Coastal Securities, 600 Navarro, Suite 350, San Antonio, Texas, 78205, or Estrada Hinojosa & Company, Inc., 1400 Frost Bank Tower, 100 West Houston Street, San Antonio, Texas 78205, by electronic mail or upon payment of reasonable copying, mailing, and handling charges.

This Official Statement speaks only as of its date, and the information contained herein is subject to change. Copies of the final Official Statement will be filed with the Municipal Securities Rulemaking Board, 1900 Duke Street, Suite 600, Alexandria, Virginia 22314.

The Bonds constitute Additional Parity Obligations, payable from and secured by a first lien on and pledge of the Gross Revenues, on parity with those City bonds that (a) are also payable from and secured by a first lien and pledge of the Gross Revenues and (b) remain outstanding subsequent to the issuance of the Bonds (such other bonds, collectively, the "Outstanding Parity Bonds"). The City has, in the Ordinance (defined herein), reserved the right to issue additional Additional Parity Obligations, which obligations, along with the Bonds and the Outstanding Parity Bonds, are referred to herein, collectively, as the "Parity Obligations". The Parity Obligations are generally described as debt obligations of the City issued thereby in support, and payable from the operational revenues, of the Airport System. Upon delivery of the Bonds, the aggregate principal amount of all outstanding Parity Obligations will equal \$167,290,000.

In addition to the Parity Obligations, the City has issued other debt obligations in support of its Airport System, including its "City of San Antonio, Texas Passenger Facility Charge and Subordinate Lien Airport System Revenue Improvement Bonds, Series 2002," currently outstanding in the aggregate principal amount of \$34,270,000, and its "City of San Antonio, Texas Passenger Facility Charge and Subordinate Lien Airport System Revenue Improvement Bonds, Series 2005", currently outstanding, in the aggregate principal amount of \$37,260,000 (such respective series of bonds, as well as any future series of bonds payable from PFC Bonds Security (defined herein) on parity therewith, collectively, the "PFC Bonds"). The PFC Bonds are payable from and secured by a first lien on and pledge of the revenues of the Passenger Facility Charge (the "PFC" and such revenues derived from the collection thereof, the "PFC Revenues"; see "THE AIRPORT SYSTEM – Capital Improvement Plan – Proposed PFC Projects" for a description of PFC Revenues) approved by the Federal Aviation Administration (the "FAA") and imposed and collected by the City with respect to its International Airport (defined herein), with additional security provided by a first lien on and pledge of the "Subordinate Net Revenues" (the respective first lien on and pledge of the PFC Revenues and the Subordinate Net Revenues, together the "PFC Bonds Security"). "Subordinate Net Revenues" represents the amount of "Net Revenues" that remain after payment of debt service on the Parity Obligations. The City has reserved the right to issue additional obligations payable from the PFC Revenues on a parity with or subordinate to the outstanding PFC Bonds. The City currently plans to issue additional PFC Bonds as a component of its Airport System CIP (defined herein) in the years 2007 and 2009, although the City is under no obligation to do so.

In addition to the foregoing, the City may, from time to time, issue (a) debt obligations secured solely by a lien on and pledge of the Subordinate Net Revenues and (b) Special Facilities Debt (defined herein) for the purpose of

providing Special Facilities (defined herein), which debt is separately secured by a pledge of certain rentals derived from the leasing of such Special Facilities. As of September 30, 2006, the only Special Facilities Debt obligations outstanding were the “City of San Antonio, Texas Special Facilities Airport Revenue Bonds, Series 1995 (The Cessna Aircraft Company Project)” in the principal amount of \$3,800,000. The City currently has no outstanding indebtedness payable solely from a lien on and pledge of Subordinate Net Revenues.

This Official Statement describes only the Bonds.

PLAN OF FINANCING

Purpose

The City is issuing the Bonds for the purposes of refunding certain of its outstanding Parity Bonds identified in Schedule I hereto (such identified Parity Bonds, the “Refunded Bonds”) and paying the costs of issuance of the Bonds.

Authority for Issuance

The Bonds will be issued in accordance with applicable law (including Chapter 22, Texas Transportation Code and Chapters 1207 and 1503, respectively, Texas Government Code); the master ordinance adopted by the City Council of the City (the “City Council”) on April 19, 2001 (the “Master Ordinance”); and an Eighth Supplement to the Master Ordinance adopted by the City Council on or about November 16, 2006 (the “Eighth Supplement” and, together with the Master Ordinance, the “Ordinance”).

Sources and Uses

The following is a summary of the application of the proceeds of the Bonds and the sources and uses of funds:

Sources of Funds	
Principal Amount of the Bonds	\$17,850,000.00
Plus Net Premium	869,923.10
Plus Accrued Interest	<u>104,125.00</u>
Total Sources of Funds	<u><u>\$18,824,048.10</u></u>
Uses of Funds	
Interest and Sinking Fund Deposit (Accrued Interest)	\$ 104,125.00
Escrow Fund Deposit	18,366,062.42
Underwriters’ Discount	114,234.55
Costs of Issuance (including Bond Insurance Premium and Surety Policy Premium)	<u>239,626.13</u>
Total Uses of Funds	<u><u>\$18,824,048.10</u></u>

Refunded Bonds

The Refunded Bonds, and interest due thereon, are to be paid on the scheduled interest payment dates or the redemption date, if any, identified on Schedule I attached hereto (the “Redemption Date”) from funds to be deposited with The Bank of New York Trust Company, National Association, Dallas, Texas (the “Escrow Agent”), pursuant to an Escrow Agreement, dated as of November 1, 2006 (the “Escrow Agreement”), between the City and the Escrow Agent.

The Ordinance provides that the City will deposit certain proceeds of the sale of the Bonds and available funds of the City with the Escrow Agent in such amounts which are necessary, when combined with the interest earnings thereon, to accomplish the discharge and final payment of the Refunded Bonds. Such funds will be held by the Escrow Agent in an escrow fund (the “Escrow Fund”) irrevocably pledged to the payment of principal of and interest on the Refunded Bonds and will be used to purchase certain obligations of the United States of America and obligations of agencies or instrumentalities of the United States, including obligations that are unconditionally guaranteed by the agency or instrumentality, that are noncallable and that were, on the date the Eighth Supplement was adopted, rated as to investment quality by a nationally recognized rating firm not less than “AAA” (the “Federal Securities”). Such

maturing principal of and interest on the Federal Securities will not be available to pay the debt service requirements on the Bonds.

Simultaneously with the issuance of the Bonds, the City will give irrevocable instructions to give the required notice to the owners of the Refunded Bonds that said bonds will be redeemed prior to their stated maturity on the Redemption Date, on which date the money held in the Escrow Fund will be made available to redeem the Refunded Bonds.

Grant Thornton LLP, Minneapolis, Minnesota (the "Verification Agent"), will verify from the information provided to them the mathematical accuracy, as of the date of the closing on the Bonds, of (1) the computations contained in the schedules provided by Coastal Securities, the Co-Financial Advisor to the City, to determine that the anticipated receipts from the Federal Securities and cash deposits listed in the schedules, to be held in escrow, will be sufficient to pay, when due, the principal, interest, and redemption premium payment requirements of the Refunded Bonds, and (2) the computations of yield on both the Federal Securities and the Bonds, contained in the aforementioned schedules, which were used by Bond Counsel in its determination that the interest on the Bonds is excludable from gross income for federal income tax purposes. The Verification Agent will express no opinion on the assumptions provided to them, nor as to the exemption from taxation of the interest on the Bonds. (See "VERIFICATION OF ARITHMETICAL AND MATHEMATICAL COMPUTATIONS" herein.)

The Escrow Agent will hold and administer the Escrow Fund and will apply the maturing principal of and interest on the Federal Securities to payments of principal of, redemption premium, and interest on the Refunded Bonds. By the deposit of the Federal Securities and cash with the Escrow Agent pursuant to the Escrow Agreement, and in reliance upon the report of the Verification Agent, Bond Counsel is of the opinion that the City will have entered into firm banking and financial arrangements for the final payment and discharge of the Refunded Bonds pursuant to the terms of the ordinance authorizing their issuance and in accordance with applicable Texas law, and that the Refunded Bonds will be deemed to be no longer outstanding, except for the purpose of being paid from funds held in the Escrow Fund. (See "FORM OF BOND COUNSEL OPINION" attached hereto as Appendix E.)

The City has covenanted in the Escrow Agreement to make timely deposits to the Escrow Fund, from lawfully available funds, of any additional amounts required to pay the principal of, redemption premium, and interest on the Refunded Bonds if for any reason the cash balance on deposit or scheduled to be on deposit in the Escrow Fund should be insufficient to make such payments.

Security for the Bonds

The Bonds are payable from and secured by an irrevocable first lien on and pledge of the Gross Revenues, on parity with the other Parity Obligations. "Gross Revenues" include all of the revenues and income of every nature and from whatever source derived by the City (but excluding grants and donations for capital purposes) from the operation and/or ownership of the Airport System, including the income earned from the investment or deposit of money in each "Fund" (except the Construction Fund) created by the Master Ordinance; provided, however, that if the net rent (excluding ground rent) from any lease is pledged to the payment of principal, interest, reserve, or other requirements in connection with revenue bonds issued by the City to provide Special Facilities for the Airport System for the lessee (or in connection with bonds issued to refund said revenue bonds) the amount of such net rent so pledged and actually used to pay such requirements does not constitute and is not considered Gross Revenues, but all ground rent, and any net rent in excess of the amounts so pledged and used, must be deposited in the Revenue Fund. Without limiting the generality of the foregoing, the term "Gross Revenues" includes all landing fees and charges, ground rentals, space rentals in buildings and all charges made to concessionaires, and all revenues of any nature derived from contracts or use agreements with airlines and other users of the Airport System and its facilities. The term Gross Revenues does not include any PFCs or any other similar Airport System-related charges that may be imposed by the City pursuant to federal law.

THE BONDS ARE SPECIAL OBLIGATIONS OF THE CITY, PAYABLE SOLELY FROM A FIRST AND PRIOR LIEN ON AND PLEDGE OF THE GROSS REVENUES OF THE AIRPORT SYSTEM. NEITHER THE TAXING POWER OF THE CITY, THE STATE OF TEXAS, OR ANY POLITICAL SUBDIVISION THEREOF, NOR ANY OTHER FUNDS OF THE CITY, ARE PLEDGED TO THE PAYMENT OF THE BONDS. NO MORTGAGE OR LIEN HAS BEEN CREATED ON THE PHYSICAL PROPERTIES

OF THE AIRPORT SYSTEM OR ANY OTHER PROPERTY OF THE CITY TO SECURE PAYMENT OF THE BONDS.

Bond Insurance

The payment of the principal of and interest on the Bonds is expected to be guaranteed by a municipal bond insurance policy delivered in conjunction with their issuance. (See "BOND INSURANCE" herein.)

Perfection of Security Interest in Gross Revenues

Chapter 1208, Texas Government Code, applies to the issuance of the Bonds and the pledge of the Gross Revenues thereto, and such pledge is, therefore, valid, effective, and perfected. Should Texas law be amended at any time while the Bonds are outstanding and unpaid, the result of such amendment being that the pledge of the Gross Revenues is to be subject to the filing requirements of Chapter 9, Texas Business & Commerce Code, in order to preserve to the registered owners of the Bonds a security interest in such pledge, the City agrees to take such measures as it determines are reasonable and necessary to enable a filing of a security interest in said pledge to occur.

DEBT SERVICE REQUIREMENTS

The following schedule reflects the total principal and interest requirements on all outstanding Parity Obligations.

Fiscal Year Ending September 30	Existing Debt Service ⁽¹⁾	Refunded Debt Service	The Bonds		Total Debt Service	Total Debt Service on all Parity Obligations
			Principal	Interest		
2007	\$ 16,997,859	\$ 2,063,663	\$ 1,465,000	\$ 595,000	\$ 2,060,000	\$ 16,994,196
2008	17,072,461	2,078,813	1,125,000	819,250	1,944,250	16,937,898
2009	18,000,949	2,064,688	1,165,000	763,000	1,928,000	17,864,261
2010	18,022,136	3,247,713	2,410,000	704,750	3,114,750	17,889,173
2011	18,508,561	3,259,488	2,540,000	584,250	3,124,250	18,373,323
2012	18,493,686	3,237,713	2,645,000	457,250	3,102,250	18,358,223
2013	18,511,636	3,258,813	2,800,000	325,000	3,125,000	18,377,823
2014	15,483,549	4,018,500	3,700,000	185,000	3,885,000	15,350,049
2015	15,529,061	-0-	-0-	-0-	-0-	15,529,061
2016	15,544,155	-0-	-0-	-0-	-0-	15,544,155
2017	7,540,080	-0-	-0-	-0-	-0-	7,540,080
2018	7,545,993	-0-	-0-	-0-	-0-	7,545,993
2019	7,558,263	-0-	-0-	-0-	-0-	7,558,263
2020	7,566,763	-0-	-0-	-0-	-0-	7,566,763
2021	7,573,475	-0-	-0-	-0-	-0-	7,573,475
2022	7,586,013	-0-	-0-	-0-	-0-	7,586,013
2023	7,593,325	-0-	-0-	-0-	-0-	7,593,325
2024	7,604,888	-0-	-0-	-0-	-0-	7,604,888
2025	7,609,650	-0-	-0-	-0-	-0-	7,609,650
2026	7,622,088	-0-	-0-	-0-	-0-	7,622,088
2027	7,635,888	-0-	-0-	-0-	-0-	7,635,888
Totals	\$255,600,479	\$23,229,391	\$17,850,000	\$4,433,500	\$22,283,500	\$254,654,588

⁽¹⁾ Includes the Refunded Bonds.

THE BONDS

General Description

The Bonds will be dated November 1, 2006 and will bear interest from such date at the rates set forth on the inside cover page hereof payable on January 1 and July 1 of each year, commencing July 1, 2007, until the stated maturity

or prior redemption thereof. The principal of and interest on the Bonds are payable in the manner described herein under “THE BONDS – Book-Entry-Only System.”

In the event the Book-Entry-Only System (described herein) is discontinued, the interest on the Bonds will be payable to the registered owner as shown on the security register maintained by the Paying Agent/Registrar relating to the Bonds (the “Register”), as of the Record Date (defined herein), by check, mailed first-class postage prepaid, to the address of such person on the security register or by such other method acceptable to the Paying Agent/Registrar requested by and at the risk and expense of the registered owner. In the event the Book-Entry-Only System is discontinued, the principal of the Bonds will be payable at stated maturity upon presentation and surrender thereof at the designated payment office of the Paying Agent/Registrar.

If the date for the payment of the principal of or interest on the Bonds is a Saturday, a Sunday, a legal holiday, or a day when banking institutions in the city where the Paying Agent/Registrar is located are authorized to close or the U.S. Post Office is not open for business, then the date for such payment will be the next succeeding day which is not such a day, and payment on such date will have the same force and effect as if made on the date payment was due.

Paying Agent/Registrar

The initial Paying Agent/Registrar is The Bank of New York Trust Company, National Association, Dallas, Texas (the “Paying Agent/Registrar”). In the Ordinance, the City covenants to provide a competent and legally qualified bank, trust company, financial institution, or other entity to act as and perform the services of Paying Agent/Registrar at all times until the Bonds are duly paid, and the City retains the right to replace the Paying Agent/Registrar. If the Paying Agent/Registrar is replaced by the City, the new Paying Agent/Registrar must accept the previous Paying Agent/Registrar’s records and act in the same capacity as the previous Paying Agent/Registrar. Any successor Paying Agent/Registrar, selected at the sole discretion of the City, must be a bank, trust company, financial institution, or other entity duly qualified and legally authorized to serve as a Paying Agent/Registrar for the Bonds. Upon a change in the Paying Agent/Registrar for the Bonds, the City is required to promptly cause written notice thereof to be sent to each registered owner of the Bonds by U.S. mail, first-class postage prepaid.

Record Date for Interest Payment

The record date for determining the person to whom the semiannual interest on the Bonds is payable on any interest payment date (the “Record Date”) is the 15th day of the month next preceding such interest payment date. In the event of a non-payment of interest on a scheduled payment date, and for 30 days thereafter, a new record date for such interest payment (a “Special Record Date”) will be established by the Paying Agent/Registrar, if and when funds for the payment of such interest have been received from the City. Notice of the Special Record Date and of the scheduled payment date of the past due interest (which must be 15 days after the Special Record Date) will be sent at least five business days prior to the Special Record Date by U.S. mail, first-class postage prepaid, to the address of each registered owner of a Bond appearing on the registration books of the Paying Agent/Registrar at the close of business on the day next preceding the date of mailing of such notice.

Bond Provisions

Transfer, Exchange, and Registration. In the event the Bonds are not in the Book-Entry-Only System, the Bonds may be registered, transferred, assigned, and exchanged on the Register only upon presentation and surrender thereof to the Paying Agent/Registrar, and such registration, transfer, and exchange will be without expense or service charge to the registered owner, except for any tax or other governmental charges required to be paid with respect to such registration, transfer, and exchange. A Bond may be assigned by the execution of an assignment form on the Bonds or by other instrument of transfer and assignment acceptable to the Paying Agent/Registrar. The new Bonds will be delivered by the Paying Agent/Registrar in lieu of the Bonds being transferred or exchanged at the designated payment office of the Paying Agent/Registrar, or sent by U.S. registered mail to the new registered owner at the registered owner’s request, risk, and expense. New Bonds issued in an exchange or transfer of the Bonds will be delivered to the registered owner or assignee of the registered owner, to the extent possible, within three business days after the receipt of the Bonds to be canceled in the exchange or transfer and the written instrument of transfer or request for exchange duly executed by the registered owner or his duly authorized agent, in form satisfactory to the Paying Agent/Registrar. New Bonds registered and delivered in an exchange or transfer will be in denominations of \$5,000 for any one stated

maturity or any integral multiple thereof and for a like aggregate principal amount, series, and rate of interest as the Bonds surrendered for exchange or transfer. (See “THE BONDS – Book-Entry-Only System” herein for a description of the system to be utilized in regard to ownership and transferability of the Bonds while the Bonds are issued under DTC’s Book-Entry-Only System.)

Limitation on Transfer. Neither the City nor the Paying Agent/Registrar will be required to transfer or exchange any Bonds during the period commencing at the close of business on the Record Date and ending at the opening of business on the next interest payment date.

Defaults and Remedies. The Master Ordinance provides that if the City defaults in the payment of principal of or interest on any Parity Obligation or a default in the performance of any duty or covenant provided by law or in the Master Ordinance and any Supplement, the owner or owners of a Parity Obligation may pursue all legal remedies afforded by the Constitution and laws of the State of Texas to compel the City to remedy such default and to prevent further default or defaults. Without in any way limiting the generality of the foregoing, the Master Ordinance expressly provides that any owner of a Parity Obligation may at law or in equity, by suit, action, mandamus, or other proceedings filed in any court of competent jurisdiction, enforce and compel performance of all duties required to be performed by the City under the Master Ordinance and any Supplement, including the making of reasonably required rates and charges for the use and services of the Airport System, the deposit of the Gross Revenues into the Funds and Accounts provided in the Master Ordinance and any Supplement, and the application of such Gross Revenues in the manner required in the Master Ordinance and any Supplement. The issuance of a writ of mandamus is controlled by equitable principles, so it rests with the discretion of the court but may not be arbitrarily refused. There is no acceleration of maturity of the Bonds in the event of default and, consequently, the remedy of mandamus may have to be relied upon from year to year. The Master Ordinance does not provide for the appointment of a trustee to represent the interest of the bondholders upon any failure of the City to perform in accordance with the terms of the Master Ordinance or any Supplement, or upon any other condition and, accordingly, all legal actions to enforce such remedies would have to be undertaken at the initiative of, and be financed by, the registered owners of the Parity Obligations. On June 30, 2006, the Texas Supreme Court ruled in *Tooke v. City of Mexia*, 197 S.W.3d 325 (Tex.2006) that a waiver of sovereign immunity in a contractual dispute must be provided for by statute in “clear and unambiguous” language. Because it is unclear whether the Texas Legislature has effectively waived the City’s sovereign immunity from a suit for money damages, Bondholders may not be able to bring such a suit against the City for breach of the Parity Obligations or the Ordinance covenants. Even if a judgment against the City could be obtained, it could not be enforced by direct levy and execution against the City’s property. Furthermore, the City is eligible to seek relief from its creditors under Chapter 9 of the U.S. Bankruptcy Code (“Chapter 9”); however, Chapter 9 provides for the recognition of a security interest represented by a specifically pledged source of revenues, such as that of the Gross Revenues. Chapter 9 also includes an automatic stay provision that would prohibit, without Bankruptcy Court approval, the prosecution of any other legal action by creditors or bondholders of an entity which has sought protection under Chapter 9. Therefore, should the City avail itself of Chapter 9 protection from creditors, the ability to enforce any other remedies available to the registered owners, other than for the pledge of Gross Revenues securing the Parity Obligations, would be subject to the approval of the Bankruptcy Court (which could require that the action be heard in Bankruptcy Court instead of other federal or state court); and the Bankruptcy Code provides for broad discretionary powers of a Bankruptcy Court in administering any proceeding brought before it. The opinion of Bond Counsel will note that all opinions relative to the enforceability of the Ordinance and the Bonds are qualified with respect to the customary rights of debtors relative to their creditors.

Defeasance. The City may discharge its obligation to the registered owners of any or all of the Bonds to pay principal and interest, within the meaning of the Ordinance when payment of the principal of and interest on such Bonds to the stated maturity thereof or to the redemption date thereof has been made, by depositing with any permitted entity, as specified in Chapter 1207, Texas Government Code, as amended, for such Bonds: (i) money sufficient to pay the principal amount of such Bonds plus interest thereon to the date of maturity or redemption, (ii) Government Obligations (as defined below) bearing interest at rates sufficient to provide for the timely payment of the principal amount of such Bonds plus interest thereon to the date of maturity or redemption, or (iii) a combination of money and Government Obligations together sufficient to make such payment.

The Ordinance provides that “Government Obligations” means the (i) direct noncallable obligations of the United States, including obligations that are unconditionally guaranteed by the United States of America; (ii) noncallable obligations of an agency or instrumentality of the United States, including obligations that are unconditionally guaranteed or insured by the agency of instrumentality and that, on the date the governing body of the

City adopts or approves the proceedings authorizing the issuance of refunding bonds, are rated as to investment quality by a nationally recognized investment rating firm not less than “AAA” or its equivalent, or (iii) noncallable obligations of a state or an agency or a county, municipality, or other political subdivision of a state that have been refunded and that, on the date the governing body of the City adopts or approves the proceedings and authorizing the issuance of refunding bonds, are rated as to investment quality by a nationally recognized investment rating firm not less than “AAA” or its equivalent.

Upon such deposit as described above, such Bonds will no longer be regarded to be outstanding or unpaid and shall no longer be entitled to the benefits and the rights afforded under the Ordinance, including (but not limited to) the pledge of the Pledged Revenues.

Ordinance Provisions

Amendments to Ordinance. *General.* The City has reserved the right to amend the Master Ordinance under the conditions permitted by Section 19 thereof. Certain amendments may be made without the consent of any holders of the Parity Obligations. Other amendments would require the consent of the holders of at least a majority in aggregate principal amount of the Parity Obligations. For a complete description of the manner in which the Master Ordinance may be amended, see Section 19 included in Appendix B attached hereto.

In addition, the City has reserved the right to amend the Eighth Supplement under the conditions permitted by Section 11 thereof. Certain amendments may be made without the consent of any holders of the Bonds. Other amendments would require the consent of the holders of at least a majority in aggregate principal amount of the Bonds. For a complete description of the manner in which the Eighth Supplement may be amended, see Section 11 thereof included in Appendix B attached hereto.

Additional Parity Obligations. The City may issue Additional Parity Obligations on a parity with all then-outstanding Parity Obligations (including the Bonds) in accordance with the provisions and upon satisfaction of the requirements set forth in Section 17 of the Master Ordinance, and is included in Appendix B attached hereto. The City may also issue obligations payable from only the Subordinate Net Revenues on a parity with or subordinate to the PFC Bonds under certain situations described in Appendix B hereto.

Subordinated Debt. While any Parity Obligations are outstanding and unpaid, the City cannot additionally encumber the Gross Revenues in any manner, except as permitted in the Master Ordinance in connection with its issuance of Additional Parity Obligations, unless said encumbrance is made junior and subordinate in all respect to the liens, pledges, covenants, and agreements of the Master Ordinance and any Supplement authorizing the issuance of any Parity Obligations; provided, however, the right of the City to issue obligations payable from a lien which is subordinated to the first lien on Gross Revenues securing the Parity Obligations, including Subordinated Debt, is specifically recognized and retained. The PFC Bonds, payable from the PFC Revenues and by a lien on and pledge of the Subordinate Net Revenues represent the only Subordinated Debt currently outstanding.

Rate Covenant Relating to Outstanding Parity Obligations. The City has covenanted in the Master Ordinance to fix, maintain, enforce, charge, and collect rentals, rates, fees, charges and amounts for the use, operation, services, facilities, and occupancy of the Airport System at levels necessary to produce in each Fiscal Year Gross Revenues at least sufficient to pay the Operation and Maintenance Expenses during each Fiscal Year and to provide an amount equal to 1.25 times the principal and interest requirements (other than capitalized interest) during each Fiscal Year on all then-outstanding Parity Obligations. If the Airport System becomes liable for any other obligations or indebtedness, the City has covenanted in the Master Ordinance to fix, maintain, enforce, charge, and collect additional rates, fees, charges and amounts for use, occupancy, services, facilities, and operation of the Airport System sufficient to establish and maintain funds for the payment thereof.

Funds and Accounts; Flow of Funds. The following paragraphs briefly describe in summary form the manner in which Gross Revenues are utilized and their priority of payment. For a complete description of the flow of funds as they relate to the Bonds, see Sections 6 through 12 of the Master Ordinance and Sections 8 and 9 of the Eighth Supplement, all of which are included in Appendix B hereto.

Revenue Fund. All Gross Revenues are credited from day to day as received to the credit of the Revenue Fund. Gross Revenues in the Revenue Fund are deposited to the credit of the other Funds and Accounts described in the Master Ordinance, in the manner and amounts hereinafter provided, and each of such Funds and Accounts have priority as to such deposits in the order as discussed in the following paragraphs.

Bond Fund. Deposits to the Bond Fund are made on or before the 25th day of each month in approximately equal monthly installments, as will be sufficient, together with any other funds on deposit therein and available for such purpose, to pay the interest or principal and interest scheduled to come due on all the Parity Obligations, or required to be redeemed prior to stated maturity, on the next interest payment date.

Bond Reserve Fund. The Bond Reserve Fund is required to contain an amount of money and investments equal in market value to the Average Annual Debt Service Requirements on all Parity Obligations (the "Required Reserve Amount"). Under the provisions of the Master Ordinance, the City, at its option, may fund all or a portion of the Bond Reserve Fund at the Required Reserve Amount by purchasing a Credit Facility that will provide funds, together with other Reserve Fund Obligations, if any, credited to the Bond Reserve Fund, at least equal to the Required Reserve Amount. The City may replace or substitute a Credit Facility for all or a portion of the cash or Eligible Investments on deposit in the Bond Reserve Fund or in substitution for or replacement of any existing Credit Facility.

As of the date hereof, the Bond Reserve Fund is fully funded in the amount required to be on deposit therein pursuant to the Ordinance through a combination of money, investments, and a Credit Facility issued in connection with the Refunded Bonds. Upon the delivery of the Bonds, Financial Security (defined herein) will deliver its debt service reserve fund surety policy (the "Surety Policy") relating to the Bonds for deposit to the Bond Reserve Fund. The coverage limits of the Surety Policy will be sufficient to account for any deficiency in the Bond Reserve Fund balance upon the cancellation of the existing Credit Facility relating to the Refunded Bonds, which cancellation will occur at the time said bonds are defeased. Upon delivery of the Surety Policy, the amount on deposit in the Bond Reserve Fund will be at least equal to the Required Reserve Amount.

Operation and Maintenance Account in the Revenue Fund. All amounts in the Revenue Fund in excess of those required to be made to the credit of the Bond Fund and the Bond Reserve Fund are deemed to constitute, and are designated as, the Operation and Maintenance Account in the Revenue Fund. The amounts in the Operation and Maintenance Account are, *first*, used to pay all Operation and Maintenance Expenses, and *second*, transferred to the Subordinated Debt Fund (at the times and in the amounts required by any Supplement to the Master Ordinance authorizing such Subordinated Debt) to provide for the payment of principal, premium, if any, and interest on, and other payments (excluding any Operation and Maintenance Expenses, but including payments to a related debt service reserve fund) incurred in connection with, any Subordinated Debt, including the PFC Bonds. Such payments and transfers described in the preceding sentence have priority over all deposits to the credit of the Capital Improvement Fund as hereinafter provided. No deposit may ever be made to the credit of the Capital Improvement Fund if any such deposit would reduce the amount on hand in the Operation and Maintenance Account to less than the budgeted or estimated Operation and Maintenance Expenses for the ensuing three calendar months.

Subordinated Debt Fund. For the sole purpose of paying the principal amount of, premium, if any, and interest on, and other payments (excluding any Operation and Maintenance Expenses, but including payments to a related debt service reserve fund) incurred in connection with Subordinated Debt, the City may create in a Supplement which authorizes the issuance of Subordinated Debt a separate fund designated as the Subordinated Debt Fund.

Capital Improvement Fund. After making all other required deposits and transfers, if any, to the Bond Fund, the Bond Reserve Fund, and the Operation and Maintenance Account in the Revenue Fund, the City will transfer the balance remaining in the Operation and Maintenance Account in the Revenue Fund at the end of each Fiscal Year and deposit the same to the credit of the Capital Improvement Fund. The Capital Improvement Fund will be used for the purposes, and with priority of claim thereon, as follows: *first*, for the payment of principal, interest, and reserve requirements on any Parity Obligations if funds on deposit in the Bond Fund and the Bond Reserve Fund are insufficient to make such payments; *second*, for the payment of principal, interest, and reserve requirements on Subordinated Debt if funds on deposit in the Subordinated Debt Fund and any related debt service reserve fund are insufficient to make such payments; *third*, for the purpose of paying the costs of improvements, enlargements, extensions, additions, replacements, repairs, or other capital expenditures related to the Airport System; and *fourth*, for any other lawful purpose related to the Airport System.

Rebate Fund. The Rebate Fund is for the sole benefit of the United States of America and will not be subject to the lien created by the Ordinances or to the claim of any other Person, including the Holders of the Bonds. Amounts deposited to the Rebate Fund, together with any investment earnings thereon, will be held in trust and applied solely as provided in section 148 of the Code.

Book-Entry-Only System

General. DTC will act as securities depository for the Bonds. The Bonds will be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered certificate will be issued for the Bonds, in the aggregate principal amount of such issue, and will be deposited with DTC. The City may decide to discontinue the use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Bonds will be printed and delivered and the Bonds will be subject to transfer, exchange, and registration provisions as set forth in the Ordinance and summarized under "THE BONDS – Bond Provisions – Registration, Transferability, and Exchange" above.

Appendix D hereto describes how ownership of the Bonds is to be transferred and how the principal of and interest on the Bonds are to be paid to and credited by DTC while the Bonds are registered in its nominee name. The information in Appendix D concerning DTC and the Book-Entry-Only System has been provided by DTC for use in disclosure documents such as this Official Statement. The City believes the source of such information to be reliable, but takes no responsibility for the accuracy or completeness thereof.

The City cannot and does not give any assurance that (i) DTC will distribute payments of debt service on the Bonds or redemption or other notices, to DTC Participants, (ii) DTC Participants or others will distribute debt service payments paid to DTC or its nominee (as the registered owner of the Bonds), or redemption or other notices, to the Beneficial Owners (as defined herein), or that they will do so on a timely basis, or (iii) DTC will serve and act in the manner described in this Official Statement. The current rules applicable to DTC are on file with the Securities and Exchange Commission, and the current procedures of DTC to be followed in dealing with DTC Participants are on file with DTC.

Use of Certain Terms in Other Sections of this Official Statement. With respect to this Official Statement, readers should understand that while the Bonds are in the Book-Entry-Only System, references in other sections of this Official Statement to "Registered Owners" should be read to include the person for which the Direct Participant or Indirect Participant acquires an interest in the Bonds, but (i) all rights of ownership must be exercised through DTC and the Book-Entry Only System and (ii) except as described above, notices that are to be given to registered owners under the Ordinance are required to be given only to DTC.

Payment Record

The City has never defaulted in payments on its bonded indebtedness.

THE AIRPORT SYSTEM

General

The City's airport system consists of the San Antonio International Airport (the "International Airport" or the "Airport") and Stinson Municipal Airport ("Stinson") (the International Airport and Stinson, collectively, the "Airport System"), both of which are owned by the City and operated by its Aviation Department (the "Department").

The International Airport, located on a 2,600-acre site that is adjacent to Loop 410 freeway and U.S. Highway 281, is eight miles north of the City's downtown business district. The International Airport consists of three runways with the main runway measuring 8,502 feet and able to accommodate the largest commercial passenger aircraft. Its two terminal buildings contain 24 second level gates. Presently, the following domestic air carriers provide service to San Antonio: American, American Eagle, Chautauqua, America West (which recently merged with US Airways), Mesa, Continental, Continental Express, Delta, Delta Connection/ASA, Delta Connection/Comair, Frontier, Midwest,

Northwest, Southwest, Trans States, United, and United Express/Skywest. Mexicana, Aeromexico, and Aerolitoral are Mexican airlines that provide passenger service to Mexico.

An Airport Master Plan for the International Airport was completed in 1998 for the purpose of facilitating Airport expansion in anticipation of meeting projected demand. The Airport Master Plan design allows for an increase from 24 to 55 gates. It is estimated that current gate facilities are being utilized at 88% of capacity (see “THE AIRPORT SYSTEM – Capital Improvement Plan” below).

The International Airport is considered a medium hub facility by the FAA. For the calendar year ended December 31, 2005, the International Airport enplaned approximately 3,708,351 passengers. Airport management has determined that of the Airport’s passenger traffic, approximately 88% is origination and destination in nature (which is important because it demonstrates strong travel to and from the City independent from any one airline’s hubbing strategies). A variety of services is available to the traveling public from approximately 245 commercial businesses including nine rental car companies which lease facilities at the International Airport and Stinson Municipal Airport (as described in more detail below).

Stinson, located on 300 acres approximately 5.2 miles southeast of the City’s downtown business district was established in 1915 and is one of the country’s first municipally owned airports. It is today the second oldest continuously operating airport in the U.S. and is the FAA’s designated general aviation reliever airport to International Airport. An Airport Master Plan for Stinson was initiated in March 2001 to facilitate the development of Stinson and to expand its role as a general aviation reliever to the International Airport. The Texas Department of Transportation accepted the Master Plan in 2002 and has recommended \$16.0 million in grant funding for capital improvements over the next ten to fifteen years. The expansion of Stinson’s facilities is also needed to take advantage of new, complementary business opportunities evolving with the synergy between Brooks City Base, KellyUSA, and the Stinson Airport. A Targeted Industries Study was completed in 2003 as part of the master planning process. The study will help facilitate development of Stinson properties through the identification of industries and businesses considered to be compatible for locating at the Stinson Municipal Airport.

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Capital Improvement Plan

General. In order to meet future airport capacity requirements, the “Airport Master Plan” for the International Airport was completed in 1998. This plan made recommendations to expand terminal and airfield capacity in an orderly manner to coincide with projected growth in passengers and aircraft operations. In fiscal year 2001-02, the City commenced implementation of a ten-year Airport “Capital Improvement Plan” (the “CIP”). Due to the terrorist attacks of September 11, 2001, and the resultant industry slowdown, however, the timing of some projects has been adjusted, and the ultimate completion of the CIP is expected to extend beyond 2015. A “Master Plan Update” is scheduled for delivery in 2010. The CIP addresses both terminal and airfield improvements, including the removal of the existing Terminal 2, parts of which are over 50 years old, and the addition of two concourses with corresponding terminal space, public parking facilities, cargo facilities, roadway improvements, and extension and improvement to two runways along with supporting taxiways and aircraft apron. The CIP over the next five years addresses primarily terminal-related improvements, parking, cargo facilities, roadway improvements, and airfield improvements. The anticipated sources of funding for the Airport’s CIP per the City’s Adopted Capital Budget for Fiscal Year 2007 through 2012 are as follows:

<u>Funding Sources</u>	<u>Anticipated Funding</u>
AIP Grants	
Entitlements	\$ 19,050,000
General Discretionary	63,225,000
Noise Discretionary	30,120,000
TxDOT	7,743,000
Passenger Facility Charges	
Pay-As-You-Go	19,302,000
PFC Secured Bonds	106,884,000
Other Funding	
Airport Funds	49,789,000
Airport Revenue (Parity) Bonds	79,420,000
Total – All Sources	<u>\$375,533,000</u>

The CIP includes capital improvements, which are generally described as follows:

<u>Improvements</u>	<u>Amount</u>
International Airport	
Terminal Area Expansion	\$217,405,000
Airfield Improvements	110,083,000
Cargo Facilities	16,735,000
Other Improvements	22,082,000
Stinson Airport	<u>9,228,000</u>
Total	<u>\$375,533,000</u>

Proposed PFC Projects. Public agencies wishing to impose Passenger Facility Charges are required to apply to the FAA for such authority and must meet certain requirements specified in the PFC Act (defined herein) and the implementing regulations issued by the FAA.

The FAA issued a “Record of Decision” on August 29, 2001 approving the City’s initial PFC application. The City, as the owner and operator of the Airport, received authority to “impose” a \$3.00 PFC and to collect, in the aggregate, approximately \$102,500,000 in PFC Revenues. On February 15, 2005, the FAA approved an application amendment increasing the PFC funding by a net amount of \$13,893,537. In addition, on February 22, 2005, the FAA approved the City’s application for an additional \$50,682,244 in PFC collections to be used for 11 new projects.

On November 21, 2001, the City began collecting a \$3.00 PFC (less an \$0.08 air carrier collection charge, which collection charge has since been raised to \$0.11) per paying passenger enplaned. A total of approximately \$167.1 million in PFC Revenues will be required to provide funding for the projects included in the Airport’s CIP. The City has received PFC “impose and use” authority, meaning that it may impose the PFC and use the resultant PFC Revenues

for all projects contemplated to be completed using future bond proceeds. The estimated PFC collection expiration date is April 1, 2016.

To date, the following projects have been approved as “impose and use” projects:

- Replace Remain Overnight (“RON”) Apron
- Implement Terminal Modifications
- Reconstruct Perimeter Road
- Construct New Concourse B
- Implement Acoustical Treatment Program
- Construct Elevated Terminal Roadway
- Upgrade Central Utility Plant
- Construct Apron – Terminal Expansion
- Install Utilities – Terminal Expansion
- Replace Two ARFF Vehicles
- Conduct Environmental Impact Statement
- Reconstruct Terminal Area Roadway
- Install Noise Monitoring Equipment
- Install Terminal and Airfield Security Improvements
- Install Airfield Electrical Improvements
- PFC Development and Administration Costs

Terminal Renovations. A comprehensive terminal renovation project was completed in 2003 to improve the quality of services provided to passengers at the International Airport. The project, which cost approximately \$29 million included a completely new appearance to the building interiors and provided state-of-art terminal amenities. Included in the terminal renovations was complete redevelopment of the concessions area to provide high-quality retail and food establishments offering a mix of regional and national brands at street prices. Concession space was expanded from 30,000 square feet to over 40,000 square feet. Through the expansion and reconfiguration of concession space, 85% of retail shops and food outlets are now at airside locations. In total, 42 retail, food and passenger service contracts were awarded. The new concessions program increased concessions revenues to the Airport from \$3.1 million in fiscal year 2002 to \$4.3 million in fiscal year 2004, and \$5.2 million in fiscal year 2005, a 68% gain in three years. On a per-boarding passenger basis, concession revenue increased from \$0.86 in fiscal year 2002 to \$1.26 for the fiscal year 2004 and \$1.43 for fiscal year 2005. Following the Airport’s implementation of its new concessions program, it was recognized by the *Airport Revenue News*’ “Best Concessions Poll.” The Airport’s concession program was voted for by a panel of judges in the airport category with less than 4 million enplanements. The Airport was honored for having the Terminal with the “Most Unique Services” and the Best Overall Concessions Program in 2004 and Best Overall Concessions Program for 2005. The publication noted the Airport’s high-tech business services, such as high-speed fax and internet, wireless capabilities and conference rooms. The Best Overall Concessions Program award is given to airports with a convenient customer-friendly layout, good visibility, attractive storefronts, and interesting themes. Also in 2004, *J. D. Power and Associates* announced through its Global Airport Satisfaction Index Study that the International Airport tied for the highest ranking in customer satisfaction among airports with less than 10 million passengers per year.

Terminal Improvements. The terminal expansion project will include a seven-gate Terminal B and a five-gate Terminal C (expandable up to eleven gates). Terminal B will replace Terminal 2, which is obsolete and will be demolished to make way for Terminal C, as well as further terminal development. Terminal C will be constructed in phases, as passenger growth and demand for gate facilities occur. Ground breaking for Terminal B is expected to take place in the spring of 2007. The present Terminal 1 will become Terminal A.

Airfield Improvements. To implement the Airport Master Plan’s airfield recommendations for capacity enhancements, a required Environmental Impact Statement (“EIS”) is underway. The EIS process was started by the FAA in 2003, with a record of decision expected in late 2006 or early 2007. The EIS will assess the environmental impacts associated with the capacity-enhancing runway/taxiway projects. Public involvement is ongoing throughout the EIS process and is considered essential to the successful completion of these projects. Airport Master Plan projects to be studied as part of the EIS include extension of Runway 3/21 and Taxiways N and O; reconstruction and upgrade of Runway 12L/30R and associated taxiways from general aviation to air carrier dimensions (of approximately 8,500 feet

by 150 feet), as well as the installation of an instrument landing system. Due to limited growth in aircraft operations, the Runway 12L/30R project was postponed and the EIS was reclassified as an Environmental Assessment ("EA"), with a record of decision expected in the fall of 2006. The EA includes the extension of Runway 3/21 and commercial property development.

In order to improve the International Airport's compatibility with its neighbors, two projects have been initiated. In October 2003, work on the installation of a Noise and Operations Monitoring System ("NOMS") began. Federal Airport Improvement Program ("AIP") grant funds will pay for 80% of the NOMS project, with the balance being provided by Airport System self-generated funds. The NOMS is composed of two main systems. These include noise monitoring and flight tracking system. The NOMS will closely track aircraft noise exposure in and around particular Airport area neighborhoods or homes and allow the Aviation Department to monitor and implement current and future noise abatement measures. Completion is anticipated for January 2007. The second compatibility project is a Land Use Study which was initiated to assist the City in planning and zoning for future development. Funded in part (80%) by a federal AIP grant, this study will establish guidelines for managing compatible land uses in areas surrounding the International Airport and Stinson. This study, which is to be based on existing airport/airfield configurations and includes a public involvement process (which began in the first quarter of 2004), has been put on hold pending the results of the EA.

Parking Improvements. The International Airport operates and maintains approximately 5,810 parking spaces and 1,230 employee parking spaces for a total of 7,040 parking spaces. A parking study was developed in 2001 for the International Airport by AGA Consulting, Inc. The study indicated that projected peak period demand for Airport parking will exceed the available supply by the end of 2006. It is estimated that 2,400 additional parking spaces will be required to satisfy projected demand over the next ten years. Future requirements for vehicle parking are currently being addressed with the design of a new long-term/short term garage. The design work is underway with ground breaking for a new five-story garage, with approximately 2,850 spaces, planned for the winter of 2006. The associated costs are included in the CIP.

Cargo Improvements. The International Airport has two designated cargo areas: the West Cargo Area, which was constructed in 1974 and refurbished in 1990, and the East Cargo Area, which was completed in 1992 and expanded in 2003. The East Cargo Area is specifically designed for use by all-cargo, overnight-express carriers. Custom-built cargo facilities in the East Cargo Area are leased to DHL and Federal Express while Eagle Global Logistics (EGL) constructed a processing facility in the year 2000. UPS expanded its facilities, relocating from the West Cargo area to the East Cargo Area in late 2005. A new belly freight facility is currently under design. Additional land has been allocated to accommodate future growth and an expansion of facilities is currently planned. Foreign trade zones exist at both cargo areas. Outbound cargo for 2004 totaled 57,465 tons and 57,944 tons for calendar years 2004 and 2005, respectively.

Airport Operations

General. The City is responsible for the issuance of revenue bonds for the Airport System and preparation of long-term financial feasibility studies for Airport System development. Direct supervision of airport operations is exercised by the Department. The Department is responsible for (i) managing, operating, and developing the International Airport, Stinson, and any other airfields which the City may control in the future; (ii) negotiating leases, agreements, and contracts; (iii) computing and supervising the collection of revenues generated by the Airport System under its management; and (iv) coordinating aviation activities under the FAA.

The International Airport has its own police and fire departments on premises. The firefighters are assigned to duty at the Airport from the City of San Antonio Fire Department, but their salaries are paid by the Department as an operation and maintenance expense of the Airport System.

The FAA has regulatory authority over navigational aid equipment, air traffic control, and operating standards at both the International Airport and Stinson.

The passage of the Aviation and Transportation Security Act ("ATSA") in November of 2001, created the Transportation Security Administration ("TSA"). The City's Aviation Department has worked closely with the TSA to

forge a new higher level of security for the traveling public. TSA employs about 300 individuals at the International Airport to meet the new federal security requirements.

The International Airport's explosive detection screening equipment is currently located in the ticket lobby areas of the two terminals; however, the Aviation Department is working with the TSA to relocate all baggage screening equipment behind the terminals in new baggage handling systems planned as part of the upcoming Terminal Expansion Project. The City entered into an agreement with the TSA for reimbursements for the costs associated with the use of Airport Police Officers at the Airport security screening checkpoints in each terminal. In fiscal year 2005, these reimbursements totaled \$370,029. The Aviation Department also utilizes five Explosive Detection Canine teams. The Police Officers, assigned with their dogs, provide additional coverage for detection of explosive materials at the Airport in the baggage pickup areas, concourses, parking, cargo and aircraft. This program is supported by the TSA with reimbursement to the Airport System at \$250,000. The International Airport's coverage is provided in addition to canine support received from San Antonio Police Department and Bexar County Sheriff's Office.

The Aviation Department has continued to work to improve its security measures. The FAA approved a grant application (80% AIP funding) in 2004 to conduct a security assessment of the International Airport's security program. This project includes an inventory of the existing security measures and an evaluation based on current and anticipated provisions of the ATSA. Recommendations for security enhancements and upgrades could include items such as perimeter fencing, air operations area access points, cargo/belly freight facilities, terminals, fueling areas, concession deliveries and air traffic control tower.

Stinson continues to experience strong growth in the number of based aircraft and volume of aircraft operations at the airport. Because of its growth, the TxDOT Aviation Division has approved grant funds for various projects at Stinson. With Airport System funds, the construction of a new facility is under way, which will give Stinson additional administrative offices, classrooms, retail space and conference rooms to accommodate and attract new business. Stinson is currently conducting an Environmental Assessment for the extension of Runway 9-27. The proposed project would provide a usable runway length of at least 5,000 feet. The additional runway length will allow Stinson to serve additional corporate aircraft under all weather conditions.

As of October 1, 2006, the Airport System employed approximately 474 employees as follows:

Administration	71	Parking Facilities	53
Airport Police	89	Airport Operations	37
Fire Rescue	29	Stinson Airport	7
Maintenance	188		

Senior Management. The chief executive officer of the Department is Mark H. Webb, Director of Aviation, who has overall responsibility for the management, administration, and planning of the Airport System. Mr. Webb has been with the City of San Antonio since 1994 and with the Department since November 2005. Mr. Webb holds a Bachelor's Degree in Agricultural Economics from Texas A&M University and a Master's Degree in Urban Administration from Trinity University. Prior to his appointment as Director of the Aviation Department, Mr. Webb served as Director of the Contract Services Department. In his role as Director of that department, he was responsible for managing a wide array of contract services, including policy and process development, contract training, solicitation reviews, initiation services for high-risk contracts, and contract compliance/monitoring services to all City departments. Mr. Webb has also had responsibility for various real estate, construction, and development activities with the City.

Dom Smith is the Assistant Aviation Director for Facilities Management and Construction. He joined the Department in 1984. He was named Assistant Director in 1999. Mr. Smith is a graduate of Texas A&M University with a degree in Agronomy. His responsibilities include airport maintenance, planning and engineering, construction management, environmental protection, and noise mitigation.

Tim O'Krongley, A.A.E., is the Acting Assistant Aviation Director for Operations. He joined the Aviation Department in 1998. He has been working in the airport industry for 18 years. Mr. O'Krongley holds a Bachelor's Degree in Aeronautical Studies and a Master's Degree in Aeronautical Science from Embry Riddle University. His responsibilities include airport operations and ground transportation, security and law enforcement, fire rescue coordination, parking facilities, and Stinson.

The interview and selection process for the new Assistant Aviation Director for Finance and Administration has been completed and an offer has been accepted. The new Assistant Director for Finance and Administration is expected to start on November 27, 2006. The responsibilities of this position include financial, property, and information systems management. Those duties are currently being shared among the Airport's senior management described in this section.

Claude Overman, C.M., is the Fiscal Planning Manager. She joined the Department in January 2003. Ms. Overman has 14 years of experience in the aviation industry. Prior to joining the Department, she served as Airworthiness Manager for Dassault Falcon Jet Corporation in Little Rock, Arkansas. Ms. Overman holds a Bachelor's Degree in Aeronautical Engineering/Aviation Management from ENAC, France, and a Master's Degree of Aeronautical Science/Aviation Management from Embry-Riddle University. Her responsibilities include airport finances, budget, and accounting.

Air Transportation Advisory Commission. The City Council appoints a 14-member Air Transportation Advisory Commission (the "Advisory Commission"). The Advisory Commission is composed of stakeholders from the aviation industry (three representatives), the travel and tourism industry (two representatives), the community (five representatives), local businesses (two representatives), Business Airport Lease (one representative) and the military (one non-voting representative). In accordance with Section 49 of the City Charter, the Advisory Commission assists the Department in an advisory capacity regarding policy affecting the City's airports and air transportation initiatives.

Budgeting. All departments of the City, including the Airport System, follow the same process for the development of annual budgets.

Each year the City's budgetary process begins with the preparation of its "Five Year Financial Forecast." The forecast is a financial and budgetary planning tool that identifies emerging issues to be encountered in the next five years that will have a fiscal impact upon the City's program of services. The forecast provides information that is utilized in the budget process by projecting revenues and anticipated expenditures under a defined set of assumptions. An important component of the forecast each year is the identification of the issues which will have a direct and indirect impact on the City as a unit of local government and as a provider of services to the community.

Following the presentation of the Five Year Financial Forecast, the City Council holds a "Goals and Objectives Work Session" at which the City Council determines its priorities for the coming budget deliberations. The budget is developed within the context of revised projected funds available and City Council priorities utilizing a target budget approach. Departments are given target budgets based on current service requirements and allowed to submit expenditure proposals within the target amount. The FY 2005 budget process was improved in many ways including providing the Mayor and City Council with eight pre-proposed budget development goal setting work sessions, scheduling an additional week for Mayor and City Council to consider the proposed budget, and restructuring the organizational analysis and city service delivery reviews with all city departments and offices.

After presentation of the City Manager's proposed budget, the City Council holds a series of work sessions to review the proposed service program details. The work sessions include a review of revenues and presentations by each department, which include a description of the significant policy issues. After considering all the recommendations and receiving input from citizens at public hearings, the City Council adopts a balanced budget.

Throughout each fiscal year, the City's staff closely monitors departmental budgets and reports to the City Council on the status of funds. Budgetary compliance is a significant tool for managing and controlling governmental activities. Therefore, conformance with budgetary limits and specifications maintained by the City is critical. The objective of these budgetary controls is to ensure compliance with legal provisions embodied in the annual appropriated budget approved by the City Council. Activities of the General Fund, Enterprise Funds (such as the Airport Fund), and the Special Revenue Funds, excluding the categorical Grants-in-Aid and Community Development Block Grant Program Funds, are included in the annual appropriated budget. October 2005 marked the beginning of the City's use of SAP, an enterprise resource management system, for the recording/reporting of all financial information.

Levels of budgetary control, that is, the levels at which expenditures cannot legally exceed appropriated amounts, are established by function and activity within individual funds. The City utilizes an encumbrance system of

accounting as one mechanism for accomplishing effective budgetary control. Encumbered amounts lapse at year-end; however, encumbrances generally are appropriated as part of the following year's budget.

Computer System Implementation

On October 1, 2004, the City implemented "SAP", an information system, to replace its outdated financial system. The City has experienced many challenges associated with the implementation of this new computer software. The City continues to aggressively pursue resolution to issues associated with the conversion to the new system and has made substantial progress.

In February 2006, the City requested that SAP perform a "health check" analysis of the core business processes and a similar assessment of the City's operational competence. Based on this analysis, SAP identified action plans related to the finance module and operation competence. These items are receiving the highest attention by the City and are the focus of a dedicated SAP Production Support Team. The timeline for implementation and completion of these action plans is May 2007 and the City, to date, has made substantial progress on these items.

Airport Activity

The following Tables 1 through 6, all of which have been prepared by the City's Aviation Department, present historical operating performance of the Airport System.

The total domestic and international enplaned passengers at the International Airport on a monthly basis, along with year to year percentage changes are shown as follows:

Total Domestic and International Enplaned Passengers **Table 1**

	2002	2003	2004	2005	2006 ⁽¹⁾
January	245,053	239,719	238,109	261,368	294,898
February	238,440	231,491	253,427	255,070	288,190
March	300,014	287,214	306,140	310,899	352,722
April	291,312	265,465	305,220	312,212	340,712
May	290,594	282,716	300,127	335,447	359,821
June	315,169	306,945	318,834	345,087	356,538
July	304,967	303,624	326,894	339,032	356,542
August	291,066	274,317	289,284	302,523	311,516
September	240,276	240,362	265,778	280,806	--
October	280,821	275,050	306,181	325,895	--
November	260,983	266,993	294,317	318,466	--
December	290,588	277,015	294,661	321,546	--
Total	<u>3,349,283</u>	<u>3,250,911</u>	<u>3,498,972</u>	<u>3,708,351</u>	<u>2,660,939</u>
Increase (Decrease) over Prior 12-Month Period	(95,592)	(98,372)	248,061	209,379	199,301 ⁽²⁾
% Increase (Decrease) over Prior 12-Month Period	(2.78%)	(2.94%)	7.63%	5.98%	8.10% ⁽²⁾

⁽¹⁾ Represents information available through August 31, 2006.

⁽²⁾ Represents increase/decrease compared to same reporting period for 2005 (January through August).

The total enplanements at the International Airport by airline for each of the last five calendar years are shown below:

Total Domestic and International Enplaned Passengers by Airline

Table 2

Airlines	2002		2003		2004		2005		2006 *	
	Number	% of Total	Number	% of Total	Number	% of Total	Number	% of Total	Number	% of Total
Aeromexico	-0-	0.00%	-0-	0.00%	-0-	0.00%	-0-	0.00%	14,967	0.56%
Aerolitoral ⁽¹⁾	--	--	6,988	0.21	8,648	0.25	9,878	0.27	5,579	0.21
American	640,345	19.12	613,909	18.88	616,664	17.62%	721,341	19.45%	531,431	19.97
American Eagle	-0-	0.00	-0-	0.00	-0-	0.00	-0-	0.00	19,307	0.73
America West	103,268	3.08	100,043	3.08	100,491	2.87	102,296	2.76	62,810	2.36
Atlantic Southeast	67,357	2.01	87,325	2.69	137,029	3.92	96,078	2.59	52,897	1.99
Comair ⁽²⁾	18,445	0.55	15,012	0.46	12,559	0.36	43,495	1.17	31,712	1.19
Continental	382,170	11.41	392,193	12.06	424,173	12.12	467,304	12.60	329,423	12.38
Delta ⁽³⁾	465,539	13.90	346,026	10.64	287,815	8.23	294,636	7.95	120,423	4.53
Frontier ⁽⁴⁾	-0-	0.00	-0-	0.00	-0-	0.00	29,631	0.80	41,804	1.57
Mexicana	61,161	1.83	58,734	1.81	63,455	1.81	67,331	1.82	47,620	1.79
Midwest	25,359	0.76	31,557	0.97	59,998	1.71	42,287	1.14	29,519	1.11
Northwest ⁽³⁾	128,592	3.84	166,843	5.13	214,801	6.14	221,414	5.97	166,527	6.26
Skywest ⁽¹⁾	--	--	38,710	1.19	34,522	0.99	96,720	2.61	81,585	3.07
Southwest	1,183,307	35.33	1,144,577	35.21	1,254,692	35.86	1,294,382	34.90	963,227	36.20
United	178,999	5.34	202,498	6.23	215,079	6.15	158,090	4.26	110,670	4.16
Other Carriers	<u>94,745</u>	<u>2.83</u>	<u>92,194</u>	<u>2.84</u>	<u>112,216</u>	<u>3.21</u>	<u>170,066</u>	<u>4.59</u>	<u>51,438</u>	<u>1.93</u>
Total	<u>3,349,283</u>	<u>100%</u>	<u>3,250,911</u>	<u>100%</u>	<u>3,498,972</u>	<u>100%</u>	<u>3,708,351</u>	<u>100%</u>	<u>2,660,939</u>	<u>100%</u>

* Year-to- date information through August 31, 2006.

(1) Data unavailable prior to 2003.

(2) Comair Airlines commenced service to the Airport in March 2002.

(3) Effective September 14, 2005, Northwest Airlines, Inc. and Delta Air Lines, Inc. and its subsidiaries filed for bankruptcy protection. (See "CERTAIN INVESTMENT CONSIDERATIONS AND RISK FACTORS – Financial Performance of Airlines Serving the Airport" herein.)

(4) Frontier Airlines commenced service to the Airport in June 2005.

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The total enplaned and deplaned international passengers at the International Airport are shown below:

Total Enplaned and Deplaned International Passengers

Table 3

<u>Months</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u> ⁽¹⁾
January	11,629	11,595	9,520	12,927	12,610
February	9,427	8,319	9,562	10,586	10,957
March	14,254	12,551	12,823	13,383	14,637
April	12,975	11,165	10,620	9,835	14,256
May	16,661	13,702	13,521	13,405	17,949
June	23,691	19,266	25,899	23,184	22,182
July	31,299	24,907	30,234	27,484	26,868
August	26,359	18,062	20,158	16,312	18,055
September	11,886	7,895	11,120	10,930	--
October	12,668	8,104	13,254	12,413	--
November	14,479	10,292	15,721	16,523	--
December	15,946	13,718	18,252	19,010	--
Total	<u>201,274</u>	<u>159,576</u>	<u>190,684</u>	<u>185,992</u>	<u>137,514</u>
Increase (Decrease) over Prior 12-Month Period	(18,078)	(41,698)	31,108	(4,692)	10,398 ⁽²⁾
% Increase (Decrease) over Prior 12-Month Period	(8.24%)	(20.72%)	19.49%	(2.46%)	8.18% ⁽²⁾

⁽¹⁾ Represents information available through August 31, 2006.

⁽²⁾ Represents increase/decrease compared to same reporting period for 2005 (January through August).

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The historical aircraft landed weight at the International Airport, in 1,000 pound units, by air carrier, in the designated calendar year is shown below. Landed weight is utilized in the computation of the Airport's landing fee.

Air Carrier Landed Weight (1,000 lbs.)

Table 4

Carrier	Calendar Year									
	2002		2003		2004		2005		2006 ⁽¹⁾	
	Weight	% of Total	Weight	% of Total	Weight	% of Total	Weight	% of Total	Weight	% of Total
Aerolitoral	22,191.5	0.40%	14,140.1	0.26%	18,012.0	0.33%	18,482.0	0.33%	10,916.3	0.28%
Aeromar	2,053.0	0.04	923.4	0.02	6,707.7	0.12	1,111.8	0.02	-0-	0.00
Aeromexico	-0-	0.00	-0-	0.00	-0-	0.00	-0-	0.00	9,904.9	0.26
Airborne	64,935.0	1.17	80,811.0	1.50	86,354.1	1.60	61,295.1	1.09	-0-	0.00
Airtrain (Postal)	-0-	0.00	-0-	0.00	-0-	0.00	-0-	0.00	-0-	0.00
America West	118,245.5	2.13	100,240.1	1.86	33,436.8	0.62	74,086.8	1.31	11,142.3	0.29
American	888,804.2	15.99	815,759.0	15.13	731,192.0	13.56	852,628.5	15.11	572,337.5	14.80
American Eagle	-0-	0.00	-0-	0.00	-0-	0.00	-0-	0.00	29,951.1	0.77
American Intl.	-0-	0.00	-0-	0.00	-0-	0.00	-0-	0.00	-0-	0.00
Atlantic Southwest	81,498.0	1.47	114,037.4	2.12	170,964.0	3.17	139,472.0	2.47	64,494.0	1.67
Comair ⁽²⁾	--	--	22,325.0	0.41	16,638.0	0.31	52,068.0	0.92	37,729.0	0.98
Continental	517,604.5	9.31	516,932.8	9.59	575,225.6	10.67	592,583.0	10.50	394,098.0	10.19
Delta	660,873.0	11.89	481,513.0	8.93	368,215.0	6.83	379,201.0	6.72	138,339.0	3.58
DHL Airways	-0-	0.00	-0-	0.00	-0-	0.00	30,080.0	0.53	54,240.0	1.40
Emery Worldwide	158.0	0.00	-0-	0.00	-0-	0.00	-0-	0.00	-0-	0.00
Federal Express	341,189.9	6.14	384,251.4	7.13	399,378.5	7.41	410,019.0	7.27	268,856.1	6.95
Frontier	-0-	0.00	-0-	0.00	-0-	0.00	49,113.0	0.87	62,668.0	1.62
Kitty Hawk	-0-	0.00	-0-	0.00	-0-	0.00	-0-	0.00	309.0	0.01
Mexicana	100,617.0	1.81	101,682.2	1.89	92,247.4	1.71	100,660.6	1.78	86,904.1	2.25
Midwest Express	54,753.7	0.98	67,588.3	1.25	91,748.7	1.70	69,928.0	1.24	48,028.0	1.24
Northwest	216,309.5	3.89	285,871.4	5.30	326,504.5	6.06	319,605.3	5.66	222,030.9	5.74
Skywest ⁽³⁾	--	--	47,141.0	0.87	38,034.0	0.71	117,984.0	2.09	96,742.0	2.50
Southwest	1,810,797.0	32.57	1,739,146.0	32.26	1,758,545.0	32.62	1,772,312.0	31.41	1,304,296.0	33.73
Sun Country	1,898.0	0.03	1,802.0	0.03	1,460.0	0.03	-0-	0.00	-0-	0.00
United	228,106.2	4.10	255,266.1	4.74	255,080.5	4.73	195,752.3	3.47	129,252.2	3.34
United Parcel	304,049.5	5.47	269,410.0	5.00	259,094.5	4.81	268,227.4	4.75	190,881.3	4.94
Other Carriers	<u>144,934.4</u>	<u>2.61</u>	<u>161,607.1</u>	<u>3.00</u>	<u>242,388.6</u>	<u>4.50</u>	<u>307,630.2</u>	<u>5.45</u>	<u>133,582.5</u>	<u>3.45</u>
	<u>5,559,017.9</u>	<u>100%</u>	<u>5,390,981.3</u>	<u>100%</u>	<u>5,416,554.9</u>	<u>100%</u>	<u>5,642,188.0</u>	<u>100%</u>	<u>3,866,702.2</u>	<u>100%</u>

⁽¹⁾ Year-to-date information through August 31, 2006.

⁽²⁾ Comair Airlines commenced service to the Airport in March 2002; data unavailable prior to 2003.

⁽³⁾ Data unavailable prior to 2003.

The following represents a summary of cargo activities at the International Airport for each of the past five years:

Enplaned Air Cargo Weights (U.S. Tons)

Table 5

Calendar Year	Mail	Freight	Total Cargo	% Change
2002	15,904.30	41,223.60	57,127.90	19.21%
2003	18,008.50	39,678.52	57,687.02	0.98
2004	16,251.42	41,213.96	57,465.38	(0.38)
2005	16,142.87	41,800.74	57,943.61	0.83
2006 ⁽¹⁾	11,792.48	30,995.55	42,788.02	12.88 ⁽²⁾

⁽¹⁾ Year-to-date information through August 31, 2006.

⁽²⁾ Represents percentage increase/decrease compared to same reporting period for 2005 (January through August).

Tables 6 and 7 reflect the historical performance of parking operations at the International Airport. The current parking rates at the International Airport are shown below.

Current Parking Rates (effective October 1, 2006)

Table 6

<u>Time Utilized</u>	<u>Short Term</u>	<u>Time Utilized</u>	<u>Long Term</u>
0 – ½ hour or fraction thereof	\$0.00	0 - ½ hour or fraction thereof	\$0.00
½ - 1 hour or fraction thereof	1.00	½ - 1 hour or fraction thereof	2.00
1 – 1 ½ hour or fraction thereof	2.00	Each additional hour or fraction thereof	2.00
1 ½ - 2 ½ hours or fraction thereof	3.00	Maximum Daily Rate (24 hours)	10.00
2 ½ - 3 ½ hours or fraction thereof	4.00		
Each additional hour or fraction thereof	2.00		
Maximum Daily Rate (24 hours)	22.00		

<u>Time Utilized</u>	<u>Shuttle</u>
0 – ¼ hour or fraction thereof	\$0.00
¼ - 1 hour or fraction thereof	2.00
Each additional hour or fraction thereof	2.00
Maximum Daily Rate (24 hours)	5.00

The historical revenues and expenses of the parking system at the Airport and parking revenues as a percentage of Gross and Net Revenues of the Airport System are shown below.

Airport Parking System Revenues

Table 7

	<u>Fiscal Years Ended September 30</u>				
	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>
Parking Revenues	\$10,955,229	\$10,400,762	\$10,692,453	\$11,415,942	\$ 13,085,884
Parking Expenses	<u>(1,987,083)</u>	<u>(2,114,736)</u>	<u>(2,252,436)</u>	<u>(2,287,311)</u>	<u>(2,546,002)</u>
Net Parking Revenues	<u>\$ 8,968,146</u>	<u>\$ 8,286,026</u>	<u>\$ 8,440,017</u>	<u>\$ 9,128,631</u>	<u>\$10,539,882</u>
Gross Parking Revenues as a % of Airport System Gross Revenues	25.52%	24.54%	24.34%	25.50%	27.74%
Net Parking Revenues as a % of Airport System Net Revenues	46.43%	41.26%	45.46%	44.31%	50.75%
Airport System Gross Revenues	\$42,928,794	\$42,377,654	\$43,930,687	\$44,763,847	\$47,180,690
Airport System Net Revenues	\$19,316,159	\$20,080,956	\$18,567,080	\$20,599,769	\$20,769,586

Source: City of San Antonio, Finance Department

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The historical financial performance of the Airport System is shown in Tables 8 and 9 and has been provided by the City's Finance Department.

A comparison of the major categories comprising Gross Revenues and Operation and Maintenance Expenses for the past five fiscal years is shown below.

Comparative Statement of Gross Revenues and Expenses

Table 8

	Fiscal Year ended September 30				
	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>
Gross Revenues					
Airline Revenues					
Scheduled Carrier Landing Fees	\$ 4,616,794	\$ 4,581,380	\$ 4,389,814	\$ 4,669,871	\$ 4,951,513
Non-Scheduled Carrier Landing Fees	772,468	793,811	800,440	878,044	1,021,264
Terminal Building Rentals ⁽¹⁾	5,979,199	7,356,692	9,465,739	8,266,382	6,302,886
FIS Space Fees	759,139	629,994	546,374	543,778	783,264
Ramp Fees	<u>376,250</u>	<u>366,875</u>	<u>377,813</u>	<u>382,500</u>	<u>385,625</u>
Subtotal Airlines Revenues	<u>\$ 12,503,850</u>	<u>\$ 13,728,752</u>	<u>\$ 15,580,180</u>	<u>\$ 14,740,585</u>	<u>\$13,444,552</u>
Non-Airline Revenues					
Concession Contracts	\$10,398,409	\$10,002,454	\$10,512,091	\$11,157,827	\$12,553,585
Parking Fees	10,955,229	10,400,762	10,692,453	11,415,942	13,085,884
Property Leases	5,720,005	5,746,096	5,969,218	6,326,041	6,479,611
Stinson Airport	163,270	170,611	218,102	123,227	83,091
Interest Income	2,984,062	1,188,675	697,233	558,781	1,386,139
Misc. Revenues	<u>203,969</u>	<u>1,140,304</u>	<u>261,410</u>	<u>441,444</u>	<u>147,828</u>
Subtotal Non-Airline Revenues	<u>\$30,424,944</u>	<u>\$28,648,902</u>	<u>\$28,350,507</u>	<u>\$30,023,262</u>	<u>\$33,736,138</u>
Total Gross Revenues	<u>\$42,928,794</u>	<u>\$42,377,654</u>	<u>\$43,930,687</u>	<u>\$44,763,847</u>	<u>\$47,180,690</u>
Operating & Maintenance Expense					
Airfield Area	\$ 1,357,513	\$ 1,384,797	\$ 1,462,907	\$ 1,403,683	\$1,351,893
Service Area	249,680	276,994	390,988	393,895	378,755
Terminal 2	1,626,325	1,896,570	2,246,782	2,074,706	2,219,679
Terminal 1	2,499,298	2,477,144	3,083,014	3,142,838	3,226,762
Fire & Rescue	2,620,549	2,279,735	2,916,359	3,097,194	3,444,348
Access	529,288	515,225	506,465	488,522	711,111
Central Plant	439,942	479,854	552,896	475,528	498,354
Commercial & Industrial	71,050	66,113	88,479	88,128	77,376
Other Buildings & Area	75,080	66,187	89,189	88,689	74,725
Parking	1,987,083	2,114,736	2,252,436	2,287,311	2,546,002
Stinson Airport	387,165	395,895	457,247	463,573	514,919
Administration	6,811,715	4,979,950	5,432,602	4,693,821	5,671,675
Main. Dir. & Control	972,242	1,021,655	1,046,729	1,053,812	1,053,701
Security	2,319,521	2,648,694	3,093,846	2,582,517	2,902,909
Operations	1,666,184	1,676,215	1,743,179	1,829,861	1,738,895
Ground Transportation	<u>-0-</u>	<u>16,934</u>	<u>489</u>	<u>-0-</u>	<u>-0-</u>
Total Operating & Maintenance Expenses	<u>\$23,612,635</u>	<u>\$22,296,698</u>	<u>\$25,363,607</u>	<u>\$24,164,078</u>	<u>\$26,411,104</u>
Net Revenues	<u>\$19,316,159</u>	<u>\$20,080,956</u>	<u>\$18,567,080</u>	<u>\$20,599,769</u>	<u>\$20,769,586</u>

⁽¹⁾ Each year, the Signatory Airlines are eligible to receive a credit against their terminal rents, in an amount equal to 50% of funds available in excess of the 25% debt service coverage requirement after the payment of all Operation and Maintenance Expenses, debt service requirements, and deposits to the bond funds. Terminal building rentals are shown net of credit.

Airport Financial Update

As part of its annual budget process, the City re-estimates revenues and expenditures for the current fiscal year. During the most recent budget process, the FY 2006 Net Revenues for the Airport were projected at \$21.2 million (exclusive of transfers to other funds and debt service).

The ratios of Gross Revenues and Net Revenues to the debt service requirements of the outstanding Parity Obligations for the past five fiscal years are shown below:

Historical Debt Service Coverage

Table 9

	Fiscal Years Ended September 30				
	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>
Gross Revenues ⁽¹⁾	\$ 42,928,794	\$42,377,654	\$43,930,687	\$44,763,847	\$47,180,690
Airline Rental Credit	<u>5,209,037</u>	<u>4,468,199</u>	<u>2,612,609</u>	<u>3,486,271</u>	<u>5,322,516</u>
Adjusted Gross Revenues	\$ 48,137,831	\$46,845,853	\$46,543,296	\$48,250,118	\$52,503,206
Operating Expenses	<u>(\$23,612,635)</u>	<u>(\$22,296,698)</u>	<u>(\$25,363,607)</u>	<u>(\$24,164,078)</u>	<u>(\$26,411,104)</u>
Net Revenue	<u>\$ 24,525,196</u>	<u>\$24,549,155</u>	<u>\$21,179,689</u>	<u>\$24,086,040</u>	<u>\$26,092,102</u>
Annual Debt Service Requirements	\$11,960,544	\$13,441,791	\$15,659,812	\$16,341,609	\$17,410,959
Gross Revenue Debt Service Coverage ⁽²⁾	4.02x	3.49x	2.97x	2.95x	3.02x
Net Revenue Debt Service Coverage	2.05x	1.83x	1.35x	1.47x	1.50x

⁽¹⁾ As reported in the City of San Antonio's audited financial statements.

⁽²⁾ Calculated using Adjusted Gross Revenues.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Operating Statistics

Operating activity pertaining to domestic and international enplaned passengers, total enplaned passengers, and total enplaned and deplaned international passengers was up for the calendar year ending December 31, 2005, as compared to the same period ending December 31, 2004. Total domestic and international enplaned passengers increased by 6%, while total enplaned and deplaned international passengers decreased by 2.46%. Air carrier landed weight increased by 4.17%. In recent years some air carriers have substituted main line aircraft for regional jets and have utilized commuter operators. This change has limited the growth in landed weight. Operating activity, as shown during the first eight months of calendar year 2006, has continued to increase with an increase in total domestic and international enplaned passengers of over 8% (when compared to the same period in calendar year 2005).

Airport Revenues

Gross revenues from fiscal year 2000 through 2005 increased by 13.52%. Over the period of 2000 through 2004 little growth occurred in non-airline revenues due to the effect of reduced passengers. This situation contributed to an increase in airline revenues of 30.9%. Although airline revenues are developed on a compensatory basis, a portion of surplus revenues are refunded to the airlines through a rental credit. Since non-airline revenues were not sufficient to offset the increase in airport operating cost over the period, the rental credit to the airlines was reduced. Another factor affecting non-airline revenues was interest income. It fell from \$2,755,869 in 2000 to \$561,483 in 2004 due to market-driven decreases in interest rates.

As passenger traffic rebounded in 2004 and 2005, however, non-airline revenues increased significantly. Some of the larger increases from 2004 to 2005 were experienced in parking gross revenues (14.6%) and concession contracts (10.24%). At the same time, airline revenues decreased by 8.8%. Even though the cost to the airlines increased over the period, it still remained fairly low on a per enplaned passenger basis. The highest point was \$4.76 in 2003, and it decreased to \$3.72 in 2005.

Airport Expenditures

Operation and Maintenance Expenses are maintained by cost centers. Operation and Maintenance Expenses increased at an average annual rate of 4.4% from fiscal year 2000 through fiscal year 2005. A significant portion of this increase has been in maintenance-related functions. This was particularly true with Terminal 2, which is the older of the two terminal buildings. Other factors which contributed to an increase in cost include added security measures, utilities, insurance, wage adjustments and IT system support. Future Operation and Maintenance Expenses are expected to increase at approximately the rate of inflation with some adjustment for passenger growth.

Increased Security Measures' Financial Impact on the Airport

Beginning in fiscal year 2004, changes to the operating budget were implemented to address the long-term effect of the additional security requirements. Annual operating expenditures are expected to total about \$971,000 for the added security measures. An estimated \$586,000 of this total is anticipated to come from federal sources and the remaining \$385,000 is funded through the Airport's Operating Fund. Future annual operating expenditures are expected to remain at approximately this level. The portion of this expense for which the Airport is responsible is incorporated into airline rates and charges.

AIRLINES' RATES AND CHARGES

The City maintains lease agreements (each a "Signatory Agreement") with airlines operating from the International Airport. The last Signatory Agreements went into effect October 1, 2001. The Signatory Agreements were extended in 2006 to expire on the earlier to occur of the date of beneficial occupancy of the new Concourse B or September 30, 2009 and retain the same basic lease provisions as those previously used. The airlines that operate under a Signatory Agreement (the "Signatory Airlines") include Aerolitoral, American, Continental, Delta, Frontier, Mexicana, Midwest, Northwest, Southwest, and United.

The Signatory Agreement provides that each Signatory Airline agrees to pay rentals, fees, and charges for its use, operation (or right to operate), and occupancy of the Airport premises and facilities, and the services appertaining thereto, in an amount which, together with rentals, fees, and charges paid by other airlines and other entities using the Airport premises and facilities, will be sufficient to produce total Gross Revenues in each fiscal year as required to satisfy the City's obligations under the rate covenant contained in the Ordinance. The Signatory Agreements establish cost centers and contain formulas and methodologies to develop rates and charges for various services as well as assuring that the rate covenant is met. Each Signatory Airline has the right to use the Airport for any lawful reasonable and appropriate activity in connection with such Signatory Airline's business of transportation by aircraft. Such use includes, among other things, terminal structures, aircraft parking ramps, runways, and taxiways. The Signatory Agreements establish procedures regarding new projects at the Airport initiated by the City and the Signatory Airlines and contain notice and consultation requirements. A Signatory Airline may not make an assignment of or sublet its rights under its Signatory Agreement without the written consent of the City, which consent may not be unreasonably withheld; provided, however, that so long as the Signatory Airline's obligations under its Signatory Agreement are assumed by the assignee, such agreement may be assigned without such consent (with prior notice being given to the Director of Aviation) to any successor in interest of the Signatory Airline with or into which the Signatory Airline may merge or consolidate, or which may succeed to the assets of the Signatory Airline or a major portion of its assets related to its air transport system. The Signatory Agreements set forth certain occurrences or events which constitute events of default thereunder and remedies on default.

Airlines that have not signed, and will not sign, the Signatory Agreement (the "Non-Signatory Airlines"), which include Aeromar, American Connection/Chautauqua, America West, America West Express/Mesa and United Express/Skywest, operate under a monthly permit. The terms and conditions of the permits are very similar to the Signatory Agreements with the exception of no benefit of a rental credit and a month-to-month continuation. Other carriers providing scheduled service operate as affiliates of Signatory Airlines, which include Delta Connection/ASA, Delta Connection/Comair, Continental Express, and Northwest AirlinK.

Airline rates and charges at the Airport are developed on a compensatory basis; however, a terminal rental credit is provided to the Signatory Airlines through the sharing of a portion of surplus revenues. For fiscal year 2007, the landing fee is \$1.11 for both Signatory Airlines and Non-Signatory Airlines. The average terminal rental rate is \$33.66 for the Signatory Airlines and \$64.81 for Non-Signatory Airlines. The aggregate cost per enplaned passenger for all airlines was \$3.72 in fiscal year 2005, is estimated at \$3.47 for fiscal year 2006, and is projected to be \$3.33 for fiscal year 2007. The decrease in cost per enplaned passenger is attributable in part to the increase in enplanements and in surplus revenues.

The City is not aware of any dispute involving the Airport over any existing or proposed rates and charges or use of Airport revenues. The City believes that the rates and charges methodology utilized by the Airport under its Signatory Agreements and the rates and charges imposed by it upon air carriers and other aeronautical users are reasonable and consistent with applicable law. Furthermore, the City believes that the Airport's use of such revenues is

consistent with the DOT and FAA proposed Revenue Retention Policy. There can be no assurance, however, that a complaint will not be brought against the City in the future challenging such methodology and the rates and charges established by the Airport and, if a judgment is rendered against the City, that rates and charges paid by aeronautical users of the Airport will not be reduced.

Certain of the Signatory Airlines (or their respective parent corporations) are subject to the information requirements of the Securities Exchange Act of 1934 and in accordance therewith file reports and other information with the Securities and Exchange Commission (the “SEC”). Only companies with securities listed on a national securities exchange, with securities traded over the counter which are registered under the Exchange Act, or which are required to file with the SEC pursuant to the information-reporting requirements will have information on file. Certain information, including financial information, as of particular dates, concerning each such Signatory Airline (or their respective parent corporations) is disclosed in certain reports and statements filed with the SEC. Such reports and statements can be inspected in the public reference facilities of the SEC at Judiciary Plaza, 450 Fifth Street, N.W., Washington, D.C., 20549, and at the SEC’s regional offices at 230 South Dearborn Street, Chicago, IL, 60604, and 75 Park Place, New York, NY, 10007, and copies of such reports and statements can be obtained from the Public Reference Section of the SEC at Judiciary Plaza, 450 Fifth Street, N.W., Washington, D.C., 20549 at prescribed rates. In addition, each domestic airline is required to file periodic reports of financial and operating statistics with the United States Department of Transportation (“DOT”). Such reports can be inspected at the following location: Offices of Aviation Information Management, Data Requirements and Public Reports Division, Research and Special Programs, Administration, Department of Transportation, 400 Seventh Street, S.W., Washington, D.C., 20590, and copies of such reports can be obtained from DOT at prescribed rates. Foreign flag airlines also provide certain information concerning their operations and financial affairs, which may be obtained from the respective airline.

FEDERAL LAW AFFECTING AIRPORT RATES AND CHARGES

General

Federal aviation law generally requires that airport fees be reasonable and that in order to receive federal grant funding, all airport generated revenues must be expended for the capital or operating costs of the airport, the local airport system, or other local facilities owned or operated by the airport owner that are directly and substantially related to air transportation of passengers or property. (See “Federal Grants-in-Aid” below). Pursuant to the requirements of the Federal Aviation Administration Authorization Act of 1994 (the “1994 Aviation Act”), the DOT and the FAA were required to promulgate regulations and policies addressing the reasonableness of airport fees. A final policy statement dated June 21, 1996 addresses airport rates and charges (the “Rates and Charges Policy”). The DOT and the FAA also issued corresponding procedural regulations setting forth an expedited hearing process to be followed in determining the reasonableness of airport rates and charges (the “Procedural Regulations”). A second policy statement regarding airport revenue retention requirements (the “Revenue Retention Policy”) issued by the FAA as mandated by 49 U.S.C. § 47107(b), finalized on February 16, 1999, reflects the FAA’s position concerning the legally permissible uses of airport revenue.

In *Air Transport Assoc. of America v. Dept. of Transportation*, 119 F.3d 38 (D.C. Cir. 1997), the Rates and Charges Policy was challenged by the Air Transport Association of America (the “ATA”), an airline trade association, and the City of Los Angeles on two grounds. First, because the Rates and Charges Policy, as drafted, provided that unless aeronautical users agreed otherwise, revenues from fees imposed for use of the airfield and public use roadways may not exceed the costs of providing such public use roadways and airfield services and airfield assets currently in use, valued at their historical cost, the City of Los Angeles argued that this methodology would force them to change their operating methods and would damage their ability to finance improvements (since they had commonly based fees for certain aeronautical facilities (such as terminals) on something other than historic costs). Second, the ATA argued that because the Rates and Charges Policy further provided that *any* “reasonable methodology” could be used to determine fees for facilities and land *not* associated with the airfield, the result would be a complete deregulation of non-airfield fees. In its review, the U.S. Court of Appeals determined that because the FAA was tasked with providing specific guidelines for determining the reasonableness of fees, and the Rates and Charges Policy provided disparate treatment of airfield and non-airfield fees, this portion of the Rates and Charges Policy was arbitrary and capricious. On rehearing, the U.S. Court of Appeals vacated the policy in part and remanded it to the DOT in its Order dated October 15, 1997.

Until DOT promulgates a new policy, the guiding principle for determining rates and charges established for use of airport assets is the federal law requirement that such charges be “reasonable.” Both the airline and airport industries have filed petitions with DOT proposing replacements for the provisions of the Rates and Charges Policy that were vacated by the U.S. Court of Appeals. On August 12, 1998, the FAA published an Advanced Notice of Proposed Rulemaking (the “Advanced Notice”), soliciting suggestions from the public about how it should replace the vacated provisions of the Rates and Charges Policy. This Advanced Notice was withdrawn on February 7, 2003, by the FAA because the DOT is considering similar rates and charges issues in its study of using market pricing to manage demand at congested airports. According to the FAA, withdrawing the notice would avoid duplication of effort and resources and would allow more complete analysis of the issues. The City can speculate on neither the DOT’s timing of delivery of this report nor its effects on airport rates and charges once delivered.

Federal Grants-in-Aid

The Airport and Airway Improvement Act of 1982, 49 U.S.C. § 47101 created the Airport Improvement Program (the “AIP”), which is a program charged with assisting the development of a nationwide system of public use airports that adequately meets the current, as well as projected, needs of civil aviation. The AIP is administered by the FAA and funded by the Federal Airport and Airway Trust Fund. This fund is financed by federal aviation user taxes. Grants are available to airport operators in the form of “entitlement” funds and “discretionary” funds. Entitlement funds are apportioned annually based upon enplaned passengers, and discretionary funds are available at the discretion of the FAA based upon a national priority system.

Annual entitlement funds will vary with the actual number of passenger enplanements at the Airport, with total appropriations for the AIP and with any revision of the existing statutory formula for calculating such funds. In addition, pursuant to the Aviation Safety and Capacity Expansion Act of 1990 (the “PFC Act”) and the Aviation Investment and Reform Act for the 21st Century (“AIR-21”), an airport’s annual federal entitlement grants are reduced by 50% when a \$3.00 PFC is imposed and reduced up to 75% when a PFC fee of more than \$3.00 is imposed. For federal fiscal years 2001 through 2005, the total amount appropriated for all airports was \$3.2 billion, \$3.3 billion, \$3.4 billion, \$3.4 billion, and \$3.471 billion, respectively. The City currently imposes a \$3.00 PFC at the Airport.

Before federal approval of any AIP grant applications can be given, eligible airports must provide written assurances that they will comply with a variety of statutorily specified conditions including obligations to operate and maintain the airport in a safe and serviceable condition, refrain from granting exclusive rights, and mitigate hazards to airspace. One additional assurance that has been the subject of some scrutiny nationally in recent years is the so-called “airport generated revenues” assurance. This assurance provides that all airport generated revenues will be expended for the capital or operating costs of the airport, the local airport system, or other local facilities owned or operated by the applicant that are directly and substantially related to air transportation of passengers or property. The City falls within the group of airports for which the “airport generated revenues” assurance applies.

No assurance can be given that federal grants-in-aid will actually be received in the amount or at the time contemplated by the City, or that the Airport will collect such federal grants-in-aid in amounts or at times sufficient to pay debt service on the Bonds.

Passenger Facility Charges

Under the PFC Act, as modified by AIR-21, the FAA may authorize a public agency to impose a PFC of \$1.00, \$2.00, \$3.00, \$4.00, or \$4.50 on each passenger enplaned at any commercial service airport (those with regularly scheduled service and enplaning 2,500 or more passengers annually) controlled by said public agency, subject to certain limitations. Public agencies wishing to impose these PFCs must apply to the FAA for such authority and meet certain requirements identified in the legislation and implementing regulation, 14 CFR Part 158, issued by the FAA.

PFCs are available to airports to finance certain projects that (i) preserve or enhance capacity, safety or security of the national air transportation system, (ii) reduce noise resulting from an airport, or (iii) furnish opportunities for enhanced competition among air carriers. Under certain circumstances, the FAA grants approval to commence collection of PFCs (“impose only” approval) before approval to spend the PFCs on approved projects (“use” approval) is granted. Approval to both collect and spend PFCs is referred to as an “impose and use” approval.

Airport Security

As a result of the September 11, 2001 terrorist attacks (the “Terrorist Attacks”), the ATSA became law on November 19, 2001. The ATSA, among other things, provided for the federalization of airport security within one year in response to the Terrorist Attacks (with an “opt-out” provision that permits the use of non-federal security screeners after three years) and created the TSA, which is now responsible for airport security. The ATSA mandates certain individual, cargo, and baggage screening requirements, security awareness programs for airport personnel, and deployment of explosive detection devices. The act also permits the deployment of air marshals on all flights and requires air marshals on all “high security risk” flights. To finance these federal security services, the ATSA required payment by the airlines of approximately \$700 million, estimated to be the cost of providing such services prior to September 11, 2001, and also imposes a passenger fee of \$2.50 for each flight segment, not to exceed \$5.00 per one-way trip. The ATSA is discussed in greater detail under “CERTAIN INVESTMENT CONSIDERATIONS AND RISK FACTORS – International Conflict and Threat of Terrorism; Increased Security Measures” below

CERTAIN INVESTMENT CONSIDERATIONS AND RISK FACTORS

General

Airline industry dynamics have a marked influence on Airport and its financial performance. Accordingly, a general understanding of the industry as a whole, as well as the various risks phased thereby, are necessary when making an informed investment decision regarding the Bonds. The following is presented not as an exhaustive list describing all factors affecting the airline industry, but rather as a short synopsis of the types of examples inherent to those entities operating within this industry. The City cannot predict the continued long term effects of the events described in this section, or of future events that are both unpredictable and unforeseeable, on air travel demands, Pledged Revenues, and/or the overall financial condition of the Airport.

Uncertainties of the Airline Industry

The past five years have been particularly difficult for the airline industry as a whole due to the convergence of multiple world and domestic events, such as the U.S. economic recession of March 2001 to November 2001, the Terrorist Attacks, the ongoing conflicts in Iraq and elsewhere in the Middle East, the perceived increase in the likelihood of additional terrorist activity, cases of severe acute respiratory syndrome, rising fuel prices, and fierce price competition among all airlines (including, particularly, low cost/low fare carriers). These events contributed to poor industry-wide performance during this period of time, as U.S. member carriers of the ATA reported aggregate losses of \$8.3 billion in 2001, \$11.3 billion in 2002, \$3.6 billion in 2003, \$19 billion in 2004, and \$5.6 billion in 2005.

These financial losses accelerated the pace of structural, industry-wide changes already underway prior to September 11, 2001. These changes include route rationalization, as well as route transfers to regional partners and reduction (or elimination) of service to unprofitable markets; schedule reductions; simplification of fleets; deferral of new aircraft delivery, employee pay cuts, reduced workforces; and an increased willingness by network carriers to match discount fares offered by low-cost carriers. Airlines have also introduced innovations in passenger service and convenience, notably the expanded use of the internet and self-service kiosks, which have greatly reduced waiting lines for boarding passes.

These measures, along with \$18 billion in federal emergency economic assistance packages made available to the airline industry by federal legislation passed in 2001 and 2003, respectively, appear to be producing the desired outcomes. Nationwide passenger traffic trends indicate a sustained recovery in air travel demand, with ATA member carriers reporting a 5.7% and 2.5% increase in revenue passenger enplanements from 2003 to 2004 and 2004 to 2005, respectively. Revenue aircraft departures reported by these same carriers were also up by 1.8% in 2004, but down by 1.6% in 2005. The ATA is currently predicting an industry-wide loss of \$0.5 billion in 2006, with an expected return to profitability in 2007.

International Conflict and Threat of Terrorism; Increased Security Measures

Concerns about the safety of airline travel and the effectiveness of security precautions, particularly in the context of international hostilities and terrorist attacks, influence passenger behavior and air travel demand. These concerns have generally intensified in the aftermath of the Terrorist Attacks and the more recent threatened activity with respect to certain flights to the United States from London UK in August 2006. Travel behavior may be affected by anxieties about the safety of flying and by the inconveniences and delays associated with more stringent screening procedures, both of which may give rise to the avoidance of air travel generally and the switching from air to surface travel. Intensified security precautions now being implemented in the United States and elsewhere, along with public acceptance of these measures and industry-wide efforts to minimize the level of inconvenience, may, however, restore public confidence in the safety of commercial aviation.

The ATSA requires that all United States airports use TSA-approved explosive detection systems to screen all checked baggage; this required equipment has been installed at the Airport. The ATSA also requires that eventually all passenger bags, mail, and cargo be screened to prevent the carriage of weapons (including chemical and biological weapons), explosives, or incendiary devices onto airplanes; however, as of the date hereof, no regulations regarding these enhanced security measures have been proposed. In terms of individual passenger screening, new explosive detection walk through trace portals have been tested. As of August 2006, the TSA had deployed trace portals at 34 airports across the United States, with deployments in additional airports ongoing. Future installation at the Airport is anticipated. Additionally, multiple federal agencies including the TSA, have been tasked with continuing research on methods for screening passengers for explosives while considering operational issues including screening times and future cost implications. The Airport continues to follow and implement security initiatives based on the policy and guidelines established by the TSA and is currently in compliance with all federally mandated security requirements. TSA has broad discretion, however, to modify security requirements from time to time.

One such modification includes the U.S. Department of Homeland Security's (the "DHS") issuance of national threat levels under a color-coded system. Heightened security measures commensurate with said declarations must be implemented, which could result in a material adverse financial impact on the Airport's operating results. For example, the Airport's operating costs increase when "Code Orange" (high terror threat) or "Code Red" (severe terror threat) declarations are issued by the DHS because of the need to exercise requisite heightened security measures. Since the institution of the alert system, the national threat level has never been raised to Code Red, but it has been raised to Code Orange a number of times (where it currently remains).

Industry consensus is that U.S. airports will be required to implement the Transportation Workers Identification Credential ("TWIC") program in the future, with the resultant costs of such program to be borne by the individual airport (including the purchase, maintenance, and operation of card readers and ongoing verification of credentials for airport workers). Implementation of the TWIC program will result in increased short and long term security costs incurred by the Airport. In addition, the TSA announced on May 17, 2006 new requirements designed to protect the more than 50,000 tons of cargo that is transported aboard passenger and all-cargo aircraft each day (the first substantial changes to air cargo regulations since 1999). Compliance with these new security measures could also increase the Airport's security costs.

The Airport's incurrence of future security costs could adversely affect its financial condition. Although the Airport has received various capital grants and reimbursements for a portion of security operating costs from the federal government in the past, there can be no assurance that it will continue to receive such federal assistance or that such assistance will be sufficient to mitigate the impact of such costs. In addition, if the airlines are required to absorb a significant amount of increased security costs, it would place an additional financial burden on an already troubled industry. The Airport cannot predict the likelihood of any future government-required security measures.

The increased awareness of the threat of terrorism, coupled with the inconvenience posed by increased security measures and the proliferation of traveling alternatives, has had and, in all likelihood for the foreseeable future, will continue to have, a negative impact on air travel in general. This is evidenced by the financial hardships experienced by the airline industry over the past five years. Congress twice acted to mitigate the effects of this difficult period, passing industry-related financial assistance legislation in both 2001 and 2003; however, there is no assurance that similar legislation will be passed in the future in the event the need again arises.

Cost of Aviation Fuel

According to the ATA, jet fuel is the second largest cost component of airline operations (after labor) and continues to be an important and uncertain determinate of an air carrier's operating economics. The price of jet fuel has historically tracked the price of crude oil, with multiple factors, including (but not limited to) difficulties in the refinery process, environmental regulations, surges in demand (both regionally and seasonally), supply disruptions (whether by natural disaster, military conflicts, or geopolitical events), and market speculation, affecting its price. The average cost of a barrel of jet fuel has increased by 168% over the past five years, averaging \$0.75 per gallon in 2001 compared to \$2.01 per gallon for the first seven months of 2006. Considering the domestic airline industry's current average consumption of approximately 53 million gallons of jet fuel per day, every \$0.01/gallon increase in fuel cost increases industry-wide annual operating expenses by \$195 million. In 2005, U.S. passenger and cargo airlines consumed more than 19.9 billion gallons of jet fuel at a cost in excess of \$33 billion.

Changes in Travel Market

Multiple factors have combined recently to alter consumer travel patterns. For example, teleconference, videoconference, and web-based meetings have improved in quality and price so that they are now oftentimes considered satisfactory alternatives to face-to-face business meetings. Recent increases in security measures, as described above, have added to the time and cost of air travel. The ATA has reported a disproportionate increase in ground versus air transportation for short-haul destinations over the recent past. Full price transparency on the Internet has increased the price sensitivity and awareness of the consumer, resulting in the lowest average airfares in the industry since 1988. These are trends that are likely to continue and will have a long-term impact on the air travel market in general.

Capacity of National Air Traffic Control and Airport Systems

Demands on the national air traffic control system continue to cause aircraft delays and restrictions, both on the number of aircraft movements in certain air traffic routes and on the number of landings and takeoffs at certain airports. These restrictions affect airline schedules and passenger traffic nationwide. The FAA is gradually automating and enhancing the computer, radar, and communications equipment of the air traffic control system and assisting in the development of additional airfield capacity through the construction of new runways and the more effective use of existing runways. Increasing demands on the national air traffic control and airport systems, however, could cause increased delays and restrictions in the future.

Regulatory Environment

The FAA has jurisdiction over flying operations generally, including personnel, aircraft, ground facilities and other technical matters, as well as certain environmental matters. Under the FAA's noise reduction regulations, the air transportation industry was required to modify substantial numbers of its existing aircraft. Airport noise remains a significant federal and local issue at certain airports, which may require substantial capital investments by the industry and/or airport operators, including the Airport, from time to time to meet applicable standards.

Bankruptcy

The City. The City may be able to file for bankruptcy under Chapter 9 of the Bankruptcy Code. Should the City become the debtor in a bankruptcy case, the Bondholders may not have a lien on Gross Revenues, Subordinate Net Revenues, and PFC Revenues received by the City after the commencement of the bankruptcy case unless either (a) the pledge of such revenues by the City constitutes a "statutory lien" within the meaning of the Bankruptcy Code or (b) such revenues constitute "special revenues" within the meaning of the Bankruptcy Code. If Gross Revenues, Subordinate Net Revenues, and PFC Revenues are not special revenues or if the Bondholders do not have a statutory lien on post-bankruptcy Gross Revenues, Subordinate Net Revenues, and PFC Revenues, delays or reductions in payments to the Bondholders may result. There may also be delays in payments to the Bondholders while a court considers these issues. Even if a court determines that Gross Revenues, Subordinate Net Revenues, and PFC Revenues are special revenues or that the Bondholders do have a lien on post-bankruptcy revenues, the court may permit the City

to spend such revenues to pay Operation and Maintenance Expenses, notwithstanding any provision of the Order to the contrary.

Airline Bankruptcy. In the event of bankruptcy proceedings involving one or more of the airlines operating at the Airport, the debtor or its bankruptcy trustee must determine within a time period determined by the court whether to assume or reject the applicable Signatory Agreement or other lease agreements or operating agreements. In the event of assumption, the debtor would be required to cure any prior defaults and to provide adequate assurance of future performances under the relevant agreements. Rejection of a lease or an executory contract by any of such airlines would give rise to an unsecured claim of the City for damages, the amount of which in the case of a lease is limited by the federal Bankruptcy Code.

The PFC Act provides that PFCs collected by the airlines constitute a trust fund held for the beneficial interest of the eligible agency imposing the PFCs; except for any handling fee or retention of interest collected on unremitted proceeds. In addition, federal regulations require airlines to account for PFCs separately and to disclose the existence and amount of funds regarded as trust funds for financial statements. The airlines, however, are permitted to commingle PFC collections with other revenues and are also entitled to retain interest earned on PFCs until such PFCs are remitted. The bankruptcy courts have not fully addressed such trust arrangements. Therefore, the Airport cannot predict how a bankruptcy court might rule on this matter in the event of bankruptcy filing by airlines operating at the Airport. It is possible that the Airport could be held to be an unsecured creditor with respect to unremitted PFCs held by an airline that has filed for bankruptcy protection. Additionally, the Airport cannot predict whether the airline that files for bankruptcy protection would have properly accounted for the PFCs owed to the Airport or whether the bankruptcy estate would have sufficient moneys to pay the Airport in full for the PFCs owed by such airline.

On October 17, 2005, amendments to the United States Bankruptcy Code, established (in part) from the recent spate of airline bankruptcies, took effect. Among other items, the amendments will force companies to reorganize and emerge from Chapter 11 protection more quickly, providing the filing company up to 18 months of protection from takeover attempts and during which it must submit a reorganization plan. The amendments also require companies to make decisions within 120 days about whether they want to reject leases of their vendors or partners.

Financial Performance of Airlines Serving the Airport

Despite the recent improved financial performance of the domestic airline industry, it is still struggling financially. Four of the ten leading U.S. airlines have filed for Chapter 11 bankruptcy protection in the last five years. Two of these, US Airways and UAL (the parent company of United Airlines) have recently emerged from bankruptcy, while the other two, Delta Airlines and Northwest Airlines (both of whom filed for bankruptcy on September 14, 2005), remain in bankruptcy restructuring and protection. Delta, United, and Northwest Airlines accounted for 11.37%, 7.07%, and 5.97%, respectively, of the Airport's 2005 passenger market share. US Airways, which now serves the Airport through its recent merger with America West Airlines, accounted for 2.83% of the Airport's 2005 passenger traffic.

Other airlines serving the Airport have experienced varying degrees of financial success and difficulty in the recent past. Southwest Airlines, the air carrier with the largest portion of the Airport's 2005 market share (34.93%) is one of the few major U.S. carriers that has remained profitable, reporting net income of \$484 million in 2005 (compared to net income of \$215 million in 2004) and \$333 million in net income for the 2006's second quarter (compared to \$144 million in net income for the same period in 2005). The AMR Corporation, American Airlines parent company (the air carrier with the Airport's second largest 2005 passenger market share at 20.44%), reported a 2005 operating loss of \$892 million (compared to an operating loss of \$821 million in 2004). AMR Corporation has, however, reported net income of \$291 million for 2006's second quarter, representing just its second profitable quarter in the last 22. Continental Airlines, which accounted for 12.66% of the Airport's 2005 passenger market share, reported a 2005 net loss of \$68 million (compared to a net loss of \$409 million in 2004), and net income of \$198 million for 2006's second quarter (compared to net income of \$100 million during the same period in 2005).

While these individual results are encouraging and in conformity with ATA's reporting of industry-wide recovery, the long term success of the airline industry remains vulnerable to the occurrence of many disruptive variables. No assurance can be given as to the financial stability or profitability of the airline industry or of any airline in particular.

The airlines and cargo carriers serving the Airport, or the respective parent corporations thereof, are subject to periodic reporting requirements of the Securities Exchange Act of 1934, as amended, and in accordance therewith, file reports or other information with the Securities and Exchange Commission (the "SEC"). Certain information, including financial information, as of particular dates concerning such airlines or their respective parent corporations is disclosed in reports and statements filed with the SEC. Such reports and statements can be inspected in the Public Reference Room of the SEC at 450 Fifth Street, N.W., Washington, D.C. 20549, and at the SEC's regional offices at 175 W. Jackson Blvd., Suite 900, Chicago, Illinois 60604 and 233 Broadway, New York, New York 10279. Copies of the reports and statements can be obtained from the Public Reference Section of the SEC, 450 Fifth Street, N.W., Washington, D.C. 20549 at prescribed rates. In addition, each airline is required to file periodic reports of financial and operating statistics with the Department of Transportation. These reports can be inspected at the following location: Office of Aviation Information Management, Data Requirements and Public Reports Division, Research and Special Programs Administration, Department of Transportation, Room 4201, 400 Seventh Street, S.W. Washington, D.C. 20590, and copies can be obtained from the Department of Transportation at prescribed rates.

INVESTMENTS

Available investable funds of the City are invested as authorized and required by the Texas Public Funds Investment Act, Chapter 2256, Texas Government Code, as amended (the "Act") and in accordance with an Investment Policy approved by the City Council of the City. The Act requires that the City establish an investment policy to ensure that City funds are invested only in accordance with State law. The City has established a written investment policy in accordance with the Act. The City's investments are managed by its Finance Director, who, in accordance with the Investment Policy, reports investment activity to the City Council. Both State law and the City's investment policies are subject to change.

Legal Investments

Under Texas law, the City is authorized to invest in (1) obligations of the United States or its agencies and instrumentalities, including letters of credit; (2) direct obligations of the State of Texas or its agencies and instrumentalities; (3) collateralized mortgage obligations directly issued by a federal agency or instrumentality of the United States, the underlying security for which is guaranteed by an agency or instrumentality of the United States; (4) other obligations, the principal and interest of which is guaranteed or insured by or backed by the full faith and credit of, the State of Texas or the United States or their respective agencies and instrumentalities; (5) obligations of states, agencies, counties, cities, and other political subdivisions of any state rated as to investment quality by a nationally recognized investment rating firm not less than A or its equivalent; (6) bonds issued, assumed or guaranteed by the State of Israel; (7) certificates of deposit meeting the requirements of the Texas Public Funds Investment Act (Chapter 2256, Texas Government Code) that are issued by or through an institution that either has its main office or a branch in Texas, and are guaranteed or insured by the Federal Deposit Insurance Corporation or the National Credit Union Share Insurance Fund, or are secured as to principal by obligations described in clauses (1) through (6) or in any other manner and amount provided by law for City deposits, (8) fully collateralized repurchase agreements that have a defined termination date, are fully secured by obligations described in clause (1), and are placed through a primary government securities dealer or a financial institution doing business in the State of Texas, (9) certain bankers' acceptances with the remaining term of 270 days or less, if the short-term obligations of the accepting bank or its parent are rated at least A-1 or P-1 or the equivalent by at least one nationally recognized credit rating agency, (10) commercial paper with a stated maturity of 270 days or less that is rated at least A-1 or P-1 or the equivalent by either (a) two nationally recognized credit rating agencies or (b) one nationally recognized credit rating agency if the paper is fully secured by an irrevocable letter of credit issued by a U.S. or state bank, (11) no-load money market mutual funds registered with and regulated by the Securities and Exchange Commission that have a dollar weighted average stated maturity of 90 days or less and include in their investment objectives the maintenance of a stable net asset value of \$1 for each share, and (12) no-load mutual funds registered with the Securities and Exchange Commission that have an average weighted maturity of less than two years, invest exclusively in obligations described in this paragraph, and are continuously rated as to investment quality by at least one nationally recognized investment rating firm of not less than "AAA" or its equivalent. In addition, bond proceeds may be invested in guaranteed investment contracts that have a defined termination date and are secured by obligations, including 26 letters of credit, of the United States or its agencies and instrumentalities in an amount at least equal to the amount of bond proceeds invested under such contract, other than the prohibited obligations described in the next succeeding paragraph.

The City may invest in such obligations directly or through government investment pools that invest solely in such obligations provided that the pools are rated no lower than “AAA” or “AAAm” or an equivalent by at least one nationally recognized rating service. The City may also contract with an investment management firm registered under the Investment Advisers Act of 1940 (15 U.S.C. Section 80b-1 et seq.) or with the State Securities Board to provide for the investment and management of its public funds or other funds under its control for a term up to two years, but the City retains ultimate responsibility as fiduciary of its assets. In order to renew or extend such a contract, the City must do so by order, ordinance, or resolution. The City may invest in securities lending programs if (i) the securities loaned under the program are 100% collateralized, a loan made under the program allows for termination at any time and a loan made under the program is either secured by (a) obligations that are described in clauses (1) through (6) above, (b) irrevocable letters of credit issued by a state or national bank that is continuously rated by a nationally recognized investment rating firm at not less than A or its equivalent, or (c) cash invested in obligations described in clauses (1) through (6) and (10) through (12) above, or an authorized investment pool; (ii) securities held as collateral under a loan are pledged to the City, held in the City's name and deposited at the time the investment is made with the City or a third party designated by the City; (iii) a loan made under the program is placed through either a primary government securities dealer or a financial institution doing business in the State of Texas; and (iv) the agreement to lend securities has a term of one year or less. The City is specifically prohibited from investing in: (1) obligations whose payment represents the coupon payments on the outstanding principal balance of the underlying mortgage-backed security collateral and pays no principal; (2) obligations whose payment represents the principal stream of cash flow from the underlying mortgage-backed security and bears no interest; (3) collateralized mortgage obligations that have a stated final maturity of greater than 10 years; and (4) collateralized mortgage obligations the interest rate of which is determined by an index that adjusts opposite to the changes in a market index.

Investment Policies

Under Texas law, the City is required to invest its funds under written investment policies that primarily emphasize safety of principal and liquidity; addresses investment diversification, yield, maturity, and the quality and capability of investment management; and includes a list of authorized investments for City funds, maximum allowable stated maturity of any individual investment, and the maximum average dollar-weighted maturity allowed for pooled fund groups. All City funds must be invested consistent with a formally adopted “investment strategy statement” that specifically addresses each funds’ investment. Each investment strategy statement will describe its objectives concerning: (1) suitability of investment type, (2) preservation and safety of principal, (3) liquidity, (4) marketability of each investment, (5) diversification of the portfolio, and (6) yield.

Under Texas law, City investments must be made “with judgment and care, under prevailing circumstances, that a person of prudence, discretion, and intelligence would exercise in the management of the person’s own affairs, not for speculation, but for investment, considering the probable safety of capital and the probable income to be derived. At least quarterly the investment officers of the City shall submit an investment report detailing: (1) the investment position of the City, (2) that all investment officers jointly prepared and signed the report, (3) the beginning market value, any additions and changes to market value and the ending value of each pooled fund group, (4) the book value and market value of each separately listed asset at the beginning and end of the reporting period, (5) the maturity date of each separately invested asset, (6) the account or fund or pooled fund group for which each individual investment was acquired, and (7) the compliance of the investment portfolio as it relates to: (a) adopted investment strategy statements and (b) state law. No person may invest City funds without express written authority from the City Council.

Additional Provisions

Under Texas law the City is additionally required to: (1) annually review its adopted policies and strategies; (2) require any investment officers’ with personal business relationships or relatives with firms seeking to sell securities to the entity to disclose the relationship and file a statement with the Texas Ethics Commission and the City Council; (3) require the registered principal of firms seeking to sell securities to the City to: (a) receive and review the City’s investment policy, (b) acknowledge that reasonable controls and procedures have been implemented to preclude imprudent investment activities, and (c) deliver a written statement attesting to these requirements; (4) perform an annual audit of the management controls on investments and adherence to the City’s investment policy; (5) provide specific investment training for the Treasurer, Chief Financial Officer and investment officers; (6) restrict reverse repurchase agreements to not more than 90 days and restrict the investment of reverse repurchase agreement funds to no greater than the term of the reverse repurchase agreement; (7) restrict its investment in mutual funds in the aggregate to

no more than 15% of its monthly average fund balance, excluding bond proceeds and reserves and other funds held for debt service, and to invest no portion of bond proceeds, reserves and funds held for debt service, in mutual funds; and (8) require local government investment pools to conform to the new disclosure, rating, net asset value, yield calculation, and advisory board requirements.

Current Investments

As of June 30, 2006, investable City funds, in the approximate amount of \$982,825,863, were 91.56% invested in obligations of the United States, or its agencies and instrumentalities, and 7.58% invested in a money market fund, with the weighted average maturity of the portfolio being less than one year. The remaining 0.86% of the City's portfolio includes convention center debt service reserve funds of \$8,499,915, which were invested in fully collateralized repurchase agreements that were fully secured by obligations of the United States or its agencies and instrumentalities. The investments and maturity terms are consistent with State law, and City's investment policy objectives are to preserve principal, limit risk, maintain diversification and liquidity, and maximize interest earnings.

The market value of such investments (as determined by the City by reference to published quotations, dealer bids, and comparable information) was approximately 99.98% of their book value. No funds of the City are invested in derivative securities; *i.e.*, securities whose rate of return is determined by reference to some other instrument, index, or commodity.

LITIGATION

General Litigation and Claims

The City is a defendant in various lawsuits and is aware of pending claims arising in the ordinary course of its municipal and enterprise activities, certain of which seek substantial damages. That litigation includes lawsuits claiming damages that allege that the City caused personal injuries and wrongful deaths; class actions and promotional practices; various claims from contractors for additional amounts under construction contracts; and property tax assessments and various other liability claims. The amount of damages in most of the pending lawsuits is capped under the Texas Tort Claims Act; therefore, the potential liability is approximated at \$13 million as of July 31, 2006. The amount of \$19.2 million is included as a component of the Reserve for claims liability. The estimated liability, including an estimate of incurred but not reported claims, is recorded in the Insurance Reserve Fund. The status of such litigation ranges from early discovery stage to various levels of appeal of judgments both for and against the City. The City intends to defend vigorously against the lawsuits; including the pursuit of all appeals; however, no prediction can be made, as of the date hereof, with respect to the liability of the City for such claims or the outcome of such lawsuits.

In the opinion of the City Attorney, it is improbable that the lawsuits now outstanding against the City could become final in a timely manner so as to have a material adverse financial impact upon the City. The City provides the following updated information related to certain lawsuits:

Charles and Tracy Pollock, individually and as next friend of Sarah Jane Pollock, a minor child v. City of San Antonio. This case alleges that benzene gas emitted from the West Avenue Landfill caused chromosomal damage to a fetus during the period of gestation, resulting in child's contraction of acute lymphoblastic leukemia. Although the jury at trial entered against a judgment of more than \$23 million against the City, the trial court immediately reduced this by \$6 million. On appeal, the Fourth Court of Appeals subsequently sided with the City and reduced the judgment further by eliminating \$10 million in exemplary damages. The remaining issue is whether personal injuries are recoverable under the theory of nuisance. The City believes they are not and that even if they are recoverable, damages are capped at \$250,000 under the Texas Tort Claims Act. The case was argued to the Texas Supreme Court on October 18, 2006.

Matthew Jackson et al. v. City of San Antonio. This is a Fair Labor Standards Act ("FLSA") lawsuit. It was brought as an opt-in class action, and 335 plaintiffs have opted in to the litigation. In general, they claim they were required to report for duty 15 minutes prior to their shift, that they had to work beyond the end of their shifts, and that they were not compensated for the time at the overtime rate, in violation of the FLSA. They claim that they were (and are) entitled to be paid at 1.5 times their regular hourly rate for off-duty assignments on City property, and they make several lesser allegations based on the FLSA as well. Plaintiffs made, and the City rejected, a settlement demand in

excess of \$15 million. The City drafted and filed a motion for summary judgment which significantly reduced the City's potential exposure. However, the Court did not decide whether the City's liability for unpaid overtime would be analyzed under a traditional 40-hour workweek, or the enhanced 43-hour overtime threshold applicable to governmental law-enforcement employers. Accordingly, the potential damages remain unquantifiable. If the Plaintiffs ultimately succeed on a preponderance of their claims, damages will most likely be in excess of \$1 million, plus reasonable and necessary attorneys' fees.

Honeywell International, Inc. v. The Clark Construction Group, Inc., d/b/a Clark Contractors, Inc., JT Construction Co., Inc. and Clark/JT Construction, a Joint Venture v. City of San Antonio. In May 1997, the City awarded a construction contract to Clark-JT Construction, a joint venture, as the prime contractor to perform labor and material for construction of the Henry B. Gonzalez Convention Center Expansion Project Phase 1b New Construction and Renovation Project. Clark-JT subsequently entered into a subcontract agreement with Honeywell to provide labor, materials equipment, and services for the Project. The Project was completed in 2001 and in March 2003, Honeywell filed a lawsuit against Clark-JT for work and excess work allegedly performed during the Project. In December 2005, Clark-JT filed this third party complaint in the amount of \$8.2 million against the City for claims related to the complaint filed against the joint venture, namely contribution/indemnity, breach of contract, breach of implied warranties, unjust enrichment/quantum meruit. This case was settled for \$3.1 million, which settlement was approved by the City Council on November 16, 2006.

Contract Negotiations

Collective Bargaining Agreement negotiations between the City of San Antonio and the San Antonio Police Officers' Association. The San Antonio Police Officers' Association ("SAPOA") and the City of San Antonio City Council approved a collective bargaining agreement ("Agreement") which provides for a term through September 30, 2006, with an evergreen clause through September 30, 2016. The parties opened negotiations on January 13, 2006 and reached a tentative agreement in October 2006. The tentative agreement was presented to the members of the SAPOA for a vote the week of October 30, 2006. The membership voted against entering into the proposed contract with the City on November 2, 2006 by a margin of 3 to 1. The parties have not discussed future negotiations at this time.

Collective Bargaining Agreement negotiations between the City of San Antonio and the International Association of Fire Fighters' Local 624. The International Association of Fire Fighters Local 624 ("Local 624") and the City of San Antonio City Council approved a collective bargaining agreement which provides for a term through September 30, 2005, with an evergreen clause through September 30, 2015.

The City and Local 624 opened negotiations during their first meeting on October 7, 2005. In December 2005, the Local 624 filed a declaratory judgment action against the City seeking an interpretation of Chapter 174 of the Texas Local Government Code. In particular, Local 624 seeks a declaration from the Court as to who can be a member of the City's bargaining team. Local 624 complained that the City's inclusion of an Assistant Fire Chief on its team creates a conflict for the Union, since it is required under Chapter 174 to represent all fire fighters, other than the Chief of the Department. On June 28, 2006, the parties appeared for a bench trial which resulted in a Judgment ruling in favor of the City, and dismissing Local 624's Petition in its entirety as to every claim for relief and finding that each party would bear its own costs and fees. Specifically the Judgment upholds the plain language of the Local Government Code, Section 174.106 stating that the parties "may designate one or more persons to negotiate or bargain on its behalf." The parties resumed negotiations on July 20, 2006. On July 28, 2006, Local 624 filed a Notice of Appeal to the Fourth Court of Appeals. The parties continued negotiations, signing a one-month extension at the end of September 2006 to continue for an additional month. On October 31, 2006, the parties reached an impasse in negotiations. The parties have not discussed possible extensions or future negotiations at this time.

CITY PENSION AND OTHER POSTEMPLOYMENT RETIREMENT BENEFIT LIABILITIES

City Pension Benefit Plans

An actuarial valuation is conducted annually on each of the City's pension benefit plans (collectively, the "City Pension Benefits Plans"), which include the Texas Municipal Retirement System and the Fire and Police Pension Fund. Such actuarial valuations, conducted in accordance with generally accepted actuarial principles and practices, summarize the funding status of each of such plans as of the respective ending dates of the prior two fiscal years, as well

as projects funding contribution requirements for the immediately succeeding fiscal year. The respective actuarial values of each plan's assets represents an adjusted value, as determined by the actuary in accordance with industry standards, and will not, therefore, equal the amounts shown in the City's statement of net assets.

As a part of its valuation of the City Pension Benefits Plans, the actuary calculates and reports any "unfunded actuarial accrued liability" ("UAAL") relating to any of such plans. The UAAL is calculated on a present value basis and includes assumptions such as (among others) rates of mortality, retirement, and disability, respectively; the estimated number of participants expected to withdraw from the subject plan; expected base salary increases; overtime rates; and investment returns. The UAAL includes liabilities for current retirees, active employees that are fully eligible, and for active employees that are not fully eligible.

Based on actuarial valuations, the City's current fire and police pension plan is funded in accordance with Texas law, but the UAAL as of October 1, 2005 was \$234.7 million. The Texas Municipal Retirement System's UAAL as of December 31, 2005 was \$166.9 million.

City's Other Postemployment Retirement Benefits

In addition to the Pension Benefits, the City provides all retired employees with certain health benefits under two postemployment retirement benefit programs. Pursuant to Governmental Accounting Standards Board (GASB) Statement No. 45, the City will be required to account for and disclose its other postemployment liability for these programs. While the provisions of GASB Statement No. 45 do not become applicable to the City until Fiscal Year 2008, the City is actively reviewing each of these plans and has had actuarial valuations performed for these programs. In addition to the disclosure provided in Note 9 of the CAFR, the following information is provided for each of the City's other postemployment retirement benefit programs.

The first program provides benefits for all non-uniformed City retirees, and for all, pre-October 1, 1989, uniformed (fire and police) retirees. This program is funded on a pay-as-you-go basis with a sharing of required costs based on the following targets: 67% by the City and 33% by the retiree. During FY 2006, the City engaged an actuarial consultant to perform an actuarial valuation of this program and assist in a review of the retirement health plan. Based on the actuarial valuation as of January 1, 2006, the UAAL was projected at \$581.3 million. Based on a review, certain changes were made to the retirement health plan and were approved on September 7, 2006, as a component of the City's FY 2007 Adopted Budget. These changes resulted in a reduction of the UAAL from \$581.3 million to approximately \$400 million.

The second program provides retirement healthcare benefits to the City's fire fighters and police officers who retired on or after October 1, 1989. The benefits of this plan are financed on a prefunded basis. Contribution and benefit levels are established pursuant to the collective bargaining agreements between the City and Fire and Police Associations, respectively. Historically, actuarial valuations of this program have been performed to determine the actuarial position of the program. The City engaged an actuarial consultant to conduct a study of the program as of October 1, 2004. This actuarial study indicated that the UAAL was \$354.2 million and that current contribution rates were not sufficient to fund the current level of retirement benefits and retire the UAAL. However, the program does not have a short-term financing problem. As of September 30, 2005, the plan had net assets available for postemployment health benefits of \$147.5 million while benefits payments for FY 2005 were \$13.6 million. See "LITIGATION-Contract Negotiations", which discloses that the City has resumed negotiations with both the police and fire unions.

Use of Assumptions and Estimates

As set forth herein, as well as in Notes 8 and 9, respectively, of the City's Comprehensive Annual Financial Report for its Fiscal Year ended September 30, 2005 (the "CAFR"; selected provisions of the CAFR are attached hereto as Appendix C), the disclosure relating to the City Pension and Retiree Health Benefits Plans are based upon certain actuarial assumptions and estimates, reasonably made based upon information available at such time, that are subject to variance. To the extent these assumptions and estimates do not materialize or are inaccurate, the financial information disclosed herein and in Notes 8 and 9, respectively, of the CAFR, including the estimated-as-compared-to-actual values of the assets and liabilities for each of the City Pension and Retiree Health Benefits Plans, could change substantially and in a materially adverse manner.

CAFR Discussion

In the CAFR, the City's existing pension and other postemployment retirement benefits ("OPEB") plans are described (see, for example, "FINANCIAL INFORMATION-Fiscal Management and Administrative Topics" included in the CAFR, as well as Notes 8 and 9 thereof discussed above). In addition, the pension schedules included in the CAFR under the heading "REQUIRED SUPPLEMENTARY INFORMATION SCHEDULES OF FUNDING PROGRESS LAST THREE FISCAL YEARS" disclose certain pension plan funding liabilities, including the UAAL. Investors should carefully review this information and the information contained herein prior to investing in the Bonds.

TAX MATTERS

Opinion

On the date of initial delivery of the Bonds, McCall, Parkhurst & Horton L.L.P., San Antonio, Texas, Bond Counsel, will render its opinion that, in accordance with statutes, regulations, published rulings, and court decisions existing on the date thereof ("Existing Law"), interest on the Bonds for federal income tax purposes will be excludable from the "gross income" of the holders thereof, except for any holder who is treated pursuant to section 147(a) of the Code as a "substantial user" of the facilities financed with proceeds of the Bonds or, a "related person" to such user. Except as stated above, Bond Counsel will express no opinion as to any other federal, state, or local tax consequences of the purchase, ownership or disposition of the Bonds. (See "FORM OF BOND COUNSEL OPINION" attached hereto as Appendix E).

In rendering its opinion, Bond Counsel will rely on (a) certain information and representations of the City, including information and representations contained in the City's federal tax certificate and (b) covenants of the City contained in the Ordinances relating to certain matters, including arbitrage and the use of the proceeds of the Bonds and the property refinanced therewith. Failure by the City to observe the aforementioned representations or covenants, could cause the interest on the Bonds to become taxable retroactively to the date of issuance.

The Code and the regulations promulgated thereunder contain a number of requirements that must be satisfied subsequent to the issuance of the Bonds in order for interest on the Bonds to be, and to remain, excludable from gross income for federal tax purposes. Failure to comply with such requirements may cause interest on the Bonds to be included in gross income retroactively to the date of issuance of the Bonds. The opinion of Bond Counsel is conditioned on compliance by the City with such requirements, and Bond Counsel has not been retained to monitor compliance with these requirements subsequent to the issuance of the Bonds.

Bond Counsel's opinion represents their legal judgment based upon their review of Existing Law and the reliance on the aforementioned information, representations, and covenants. Bond Counsel's opinion is not a guarantee of a result. Existing Law is subject to change by the Congress and to subsequent judicial and administrative interpretation by the courts and the Department of Treasury. There can be no assurance that Existing Law or the interpretation thereof will not be changed in a manner which would adversely affect the tax treatment of the purchase, ownership, or disposition of the Bonds.

A ruling was not sought from the Internal Revenue Service (the "IRS") by the City with respect to the Bonds or the projects to be refinanced with proceeds of the Bonds. No assurances can be given as to whether or not the IRS will commence an audit of the Bonds, or as to whether the IRS would agree with the opinion of Bond Counsel. If an audit is commenced, under current procedures the IRS is likely to treat the City as the taxpayer and the Bondholders may have no right to participate in such procedure. No additional interest will be paid upon any determination of taxability.

Federal Income Tax Accounting Treatment of Original Issue Discount

The initial public offering price to be paid for one or more maturities of the Bonds (the "Original Issue Discount Bonds") may be less than the principal amount thereof or one or more periods for the payment of interest on the Bonds may not be equal to the accrual period or be in excess of one year. In such event, the difference between (i) the "stated redemption price at maturity" of each Original Issue Discount Bond and (ii) the initial offering price to the

public of such Original Issue Discount Bond would constitute original issue discount. The “stated redemption price at maturity” means the sum of all payments to be made on the bonds less the amount of all periodic interest payments. Periodic interest payments are payments which are made during equal accrual periods (or during any unequal period if it is the initial or final period) and which are made during accrual periods which do not exceed one year.

Under Existing Law, any owner who has purchased such Original Issue Discount Bond in the initial public offering is entitled to exclude from gross income (as defined in section 61 of the Code) an amount of income with respect to such Original Issue Discount Bond equal to that portion of the amount of such original issue discount allocable to the accrual period. For a discussion of certain collateral federal tax consequences, see discussion set forth below.

In the event of the redemption, sale, or other taxable disposition of such Original Issue Discount Bond prior to stated maturity, however, the amount realized by such owner in excess of the basis of such Original Issue Discount Bond in the hands of such owner (adjusted upward by the portion of the original issue discount allocable to the period for which such Original Issue Discount Bond was held by such initial owner) is includable in gross income.

Under Existing Law, the original issue discount on each Original Issue Discount Bond is accrued daily to the stated maturity thereof (in amounts calculated as described below for each six-month period ending on the date before the semiannual anniversary dates of the date of the Bonds and ratably within each such six-month period) and the accrued amount is added to an initial owner’s basis for such Original Issue Discount Bond for purposes of determining the amount of gain or loss recognized by such owner upon the redemption, sale or other disposition thereof. The amount to be added to basis for each accrual period is equal to (a) the sum of the issue price and the amount of original issue discount accrued in prior periods multiplied by the yield to stated maturity (determined on the basis of compounding at the close of each accrual period and properly adjusted for the length of the accrual period) less (b) the amounts payable as current interest during such accrual period on such Original Issue Discount Bond.

The federal income tax consequences of the purchase, ownership, redemption, sale, or other disposition of Original Issue Discount Bonds which are not purchased in the initial offering at the initial offering price may be determined according to rules which differ from those described above. All owners of Original Issue Discount Bonds should consult their own tax advisors with respect to the determination for federal, state, and local income tax purposes of the treatment of interest accrued upon redemption, sale, or other disposition of such Original Issue Discount Bonds and with respect to the federal, state, local, and foreign tax consequences of the purchase, ownership, redemption, sale, or other disposition of such Original Issue Discount Bonds.

Collateral Federal Income Tax Consequences

The following discussion is a summary of certain collateral federal income tax consequences resulting from the purchase, ownership, or disposition of the Bonds. This discussion is based on Existing Law, all of which are subject to change or modification, retroactively.

The following discussion is applicable to investors, other than those who are subject to special provisions of the Code, such as financial institutions, property and casualty insurance companies, life insurance companies, individual recipients of Social Security or Railroad Retirement benefits, individuals allowed an earned income credit, certain S corporations with accumulated earnings and profits and excess passive investment income, foreign corporations subject to the branch profits tax, and taxpayers who may be deemed to have incurred or continued indebtedness to purchase tax-exempt obligations.

INVESTORS, INCLUDING THOSE WHO ARE SUBJECT TO SPECIAL PROVISIONS OF THE CODE, SHOULD CONSULT THEIR OWN TAX ADVISORS AS TO THE TAX TREATMENT WHICH MAY BE ANTICIPATED TO RESULT FROM THE PURCHASE, OWNERSHIP, AND DISPOSITION OF TAX-EXEMPT OBLIGATIONS BEFORE DETERMINING WHETHER TO PURCHASE THE BONDS.

Interest on the Bonds is an item of tax preference, as defined in section 57(a)(5) of the Code, for purposes of determining the alternative minimum tax imposed on individuals and corporations by section 55 of the Code.

Under section 6012 of the Code, holders of tax-exempt obligations, such as the Bonds, may be required to disclose interest received or accrued during each taxable year on their returns of federal income taxation.

Section 1276 of the Code provides for ordinary income tax treatment of gain recognized upon the disposition of a tax-exempt obligation, such as the Bonds, if such obligation was acquired at “market discount” and if the fixed maturity of such obligation is equal to, or exceeds, one year from the date of issue. Such treatment applies to “market discount bonds” to the extent such gain does not exceed the accrued market discount of such bonds; although for this purpose, a de minimis amount of market discount is ignored. A “market discount bond” is one which is acquired by the holder at a purchase price which is less than the stated redemption price at maturity or, in the case of a bond issued at an original issue discount, the “revised issue price” (i.e., the issue price plus accrued original issue discount). The “accrued market discount” is the amount which bears the same ratio to the market discount as the number of days during which the holder holds the obligation bears to the number of days between the acquisition date and the final maturity date.

State, Local, and Foreign Taxes

Investors should consult their own tax advisors concerning the tax implications of the purchase, ownership, or disposition of the Bonds under applicable state or local laws. Foreign investors should also consult their own tax advisors regarding the tax consequences unique to investors who are not United States persons.

REGISTRATION AND QUALIFICATION OF BONDS FOR SALE

The sale of the Bonds has not been registered under the federal Securities Act of 1933, as amended, in reliance upon the exemption provided thereunder by Section 3(a)(2); and the Bonds have not been qualified under the Securities Act of Texas in reliance upon various exemptions contained therein; nor have the Bonds been qualified under the securities acts of any other jurisdiction. The City assumes no responsibility for qualification of the Bonds under the securities laws of any jurisdiction in which the Bonds may be sold, assigned, pledged, hypothecated, or otherwise transferred. This disclaimer of responsibility for qualification for sale or other disposition of the Bonds must not be construed as an interpretation of any kind with regard to the availability of any exemption from securities registration provisions.

LEGAL INVESTMENTS AND ELIGIBILITY TO SECURE PUBLIC FUNDS IN TEXAS

Section 1201.041 of the Public Security Procedures Act (Chapter 1201, Texas Government Code) provides that the Bonds are negotiable instruments governed by Chapter 8, Texas Business and Commerce Code, and are legal and authorized investments for insurance companies, fiduciaries, and trustees, and for the sinking funds of municipalities or other political subdivisions or public agencies of the State of Texas. With respect to investment in the Bonds by municipalities or other political subdivisions or public agencies of the State of Texas, the Public Funds Investment Act, Chapter 2256, Texas Government Code, requires that the Bonds be assigned a rating of “A” or its equivalent as to investment quality by a national rating agency. See “RATINGS” herein. In addition, various provisions of the Texas Finance Code provide that, subject to a prudent investor standard, the Bonds are legal investments for state banks, savings banks, trust companies with at least \$1 million of capital, and savings and loan associations. The Bonds are eligible to secure deposits of any public funds of the State, its agencies, and its political subdivisions, and are legal security for those deposits to the extent of their market value.

The City has made no investigation of other laws, rules, regulations, or investment criteria which might apply to such institutions or entities or which might limit the suitability of the Bonds for any of the foregoing purposes or limit the authority of such institutions or entities to purchase or invest in the Bonds for such purposes. The City has made no review of laws in other states to determine whether the Bonds are legal investments for various institutions in those states.

LEGAL MATTERS

On the Closing Date the City will furnish the Underwriters with a complete transcript of proceedings incident to the authorization and issuance of the Bonds, including the unqualified approving legal opinion of the Attorney General of the State of Texas to the effect that the Bonds are valid and legally binding obligations of the City, and based

upon examination of such transcript of proceedings, the legal opinion of Bond Counsel to the effect that the Bonds are valid and legally binding obligations of the City and, subject to the qualifications set forth herein under “TAX MATTERS,” the interest on the Bonds is excludable from the gross income of the owners thereof for federal income tax purposes under existing statutes, published rulings, regulations, and court decisions. The customary closing papers, including a certificate to the effect that no litigation of any nature has been filed or is then pending to restrain the issuance and delivery of the Bonds, or which would affect the provision made for their payment or security, or in any manner questioning the validity of the Bonds will also be furnished. In its capacity as Bond Counsel, McCall, Parkhurst & Horton L.L.P., has reviewed the information appearing in this Official Statement under the captions “PLAN OF FINANCING,” “THE BONDS” (other than under the subsections “Book-Entry-Only System” and “Payment Record” as to which no view will be expressed), “TAX MATTERS,” “REGISTRATION AND QUALIFICATION OF BONDS FOR SALE,” “LEGAL INVESTMENTS AND ELIGIBILITY TO SECURE PUBLIC FUNDS IN TEXAS,” and “LEGAL MATTERS” to determine whether such information fairly summarizes the material and documents referred to therein and is correct as to matters of law. Bond Counsel has not, however, independently verified any of the factual information contained in this Official Statement nor has it conducted an investigation of the affairs of the City for the purpose of passing upon the accuracy or completeness of this Official Statement. No person is entitled to rely upon Bond Counsel’s limited participation as an assumption of responsibility for, or an expression of opinions of any kind with regard to the accuracy or completeness of any of the information contained herein. The legal fees to be paid Bond Counsel for services rendered in connection with the issuance of the Bonds are contingent on issuance and delivery of the Bonds. The legal opinion of Bond Counsel will be printed on the definitive Bonds, if any, and the form of such opinion is attached hereto as Appendix E. Certain legal matters will be passed upon for the City by the City Attorney. Certain legal matters will be passed upon for the Underwriters by their counsel, Winstead Sechrest & Minick P.C., San Antonio, Texas.

Neither the Attorney General, Bond Counsel, the City Attorney, nor Underwriters’ Counsel has been engaged to investigate or verify, and accordingly neither will express any opinion concerning, the financial condition or capabilities of the City or the sufficiency of the security for, or the value or marketability of, the Bonds.

The various legal opinions to be delivered concurrently with the delivery of the Bonds express the professional judgment of the attorneys rendering the opinions as to the legal issues explicitly addressed therein. In rendering a legal opinion, the attorney does not become an insurer or guarantor of that expression of professional judgment, of the transaction opined upon, or of the future performance of the parties to the transaction. Nor does the rendering of an opinion guarantee the outcome of any legal dispute that may arise out of the transaction.

McCall Parkhurst & Horton L.L.P. represents certain of the Underwriters from time to time on various legal matters; however, it is not representing any of the Underwriters in connection with the issuance of the Bonds. Winstead Sechrest & Minick P.C. represents the City from time to time on certain legal matters; however, it is not representing the City in connection with the issuance of the Bonds.

BOND INSURANCE

Bond Insurance Policy

Concurrently with the issuance of the Bonds, Financial Security Assurance Inc. (“Financial Security”) will issue its Municipal Bond Insurance Policy for the Bonds (the “Policy”). The Policy guarantees the scheduled payment of principal of and interest on the Bonds when due as set forth in the form of the Policy included as Exhibit F to this Official Statement.

The Policy is not covered by any insurance security or guaranty fund established under New York, California, Connecticut or Florida insurance law.

Financial Security Assurance Inc.

Financial Security is a New York domiciled financial guaranty insurance company and a wholly owned subsidiary of Financial Security Assurance Holdings Ltd. (“Holdings”). Holdings is an indirect subsidiary of Dexia, S.A., a publicly held Belgian corporation, and of Dexia Credit Local, a direct wholly-owned subsidiary of Dexia, S.A.

Dexia, S.A., through its bank subsidiaries, is primarily engaged in the business of public finance, banking and asset management in France, Belgium and other European countries. No shareholder of Holdings or Financial Security is liable for the obligations of Financial Security.

At September 30, 2006, Financial Security's combined policyholders' surplus and contingency reserves were approximately \$2,581,107,000 and its total net unearned premium reserve was approximately \$1,992,163,000 in accordance with statutory accounting principles. At September 30, 2006, Financial Security's consolidated shareholder's equity was approximately \$3,058,987,000 and its total net unearned premium reserve was approximately \$1,590,538,000 in accordance with generally accepted accounting principles.

The consolidated financial statements of Financial Security included in, or as exhibits to, the annual and quarterly reports filed after December 31, 2005 by Holdings with the Securities and Exchange Commission are hereby incorporated by reference into this Official Statement. All financial statements of Financial Security included in, or as exhibits to, documents filed by Holdings pursuant to Section 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934 after the date of this Official Statement and before the termination of the offering of the Bonds shall be deemed incorporated by reference into this Official Statement. Copies of materials incorporated by reference will be provided upon request to Financial Security Assurance Inc.: 31 West 52nd Street, New York, New York 10019, Attention: Communications Department (telephone (212) 826-0100).

The Policy does not protect investors against changes in market value of the Bonds, which market value may be impaired as a result of changes in prevailing interest rates, changes in applicable ratings or other causes. Financial Security makes no representation regarding the Bonds or the advisability of investing in the Bonds. Financial Security makes no representation regarding the Official Statement, nor has it participated in the preparation thereof, except that Financial Security has provided to the Issuer the information presented under this caption for inclusion in the Official Statement.

RATINGS

Moody's Investors Service ("Moody's"), Standard & Poor's, a Division of The McGraw-Hill Corporation ("S&P"), and FitchRatings ("Fitch") are expected to rate the Bonds "Aaa", "AAA", and "AAA", respectively, based on final delivery of the Policy on the Closing Date. Underlying ratings given to the Bonds are "A1" by Moody's; "A+" by S&P; and "A+" by Fitch. An explanation of the significance of such ratings may be obtained from Moody's, S&P, or Fitch. The rating of the Bonds by Moody's, S&P, and Fitch reflects only the views of said companies at the time the ratings are given, and the City makes no representations as to the appropriateness of the ratings. There is no assurance that the ratings will continue for any given period of time, or that the ratings will not be revised downward or withdrawn entirely by Moody's, S&P, and Fitch if, in the judgment of said companies, circumstances so warrant. Any such downward revision or withdrawal of the ratings may have an adverse effect on the market price of the Bonds.

CONTINUING DISCLOSURE OF INFORMATION

In the Ordinance, the City has made the following agreement for the benefit of the holders and Beneficial Owners of the Bonds. The City is required to observe the agreement for so long as it remains obligated to advance funds to pay the Bonds. Under the agreement, the City will be obligated to provide certain updated financial information and operating data annually, and timely notice of specified material events, to certain information vendors. This information will be available to securities brokers and others who subscribe to receive the information from the vendors.

Annual Reports

Under Texas law, including, but not limited to, Chapter 103, Texas Local Government Code, the City must keep its fiscal records in accordance with generally accepted accounting principles, must have its financial accounts and records audited by a certified public accountant, and must file each audit report with the City Clerk. The City's fiscal records and audit reports are available for public inspection during the regular business hours of the City Clerk. Additionally, upon the filing of these financial statements and the annual audit, these documents are subject to the Texas Public Information Act, Texas Government Code, Chapter 552. Thereafter, any person may obtain copies of these

documents upon submission of a written request to the City Clerk, City of San Antonio, Texas, 100 Military Plaza, San Antonio, Texas, 78205, and upon paying the applicable charges allowed by the Public Information Act for providing this information.

The City will provide certain updated financial information and operating data to certain information vendors annually. The information to be updated includes all quantitative financial information and operating data with respect to the City of the general type included in this Official Statement indicated as Tables 1-9 and in Appendix C. The City will update and provide this information within six months after the end of each fiscal year. The City will provide the updated information to each Nationally Recognized Municipal Securities Information Repository (“NRMSIR”) and to any State Information Depository (“SID”) that is designated by the State of Texas and approved by the staff of the SEC.

The City may provide updated information in full text or may incorporate by reference certain other publicly available documents, as permitted by SEC Rule 15c2-12 (the “Rule”). The updated information will include audited financial statements, if the City commissions an audit and it is completed by the required time. If audited financial statements are not available by the required time, the City will provide unaudited information within the required time and audited financial statements when and if the audit report becomes available. Any such financial statements will be prepared in accordance with the accounting principles described in Appendix C or such other accounting principles as the City may be required to employ from time to time pursuant to State law or regulation.

The City’s fiscal year ends September 30. Accordingly, it must provide updated information by March 31 in each year, unless the City changes its fiscal year. If the City changes its fiscal year, it will notify each NRMSIR and any SID of the change.

Material Event Notices

The City will also provide timely notices of certain events to certain information vendors. The City will provide notice of any of the following events with respect to the Bonds, if such event is material to a decision to purchase or sell Bonds: (1) principal and interest payment delinquencies; (2) non-payment related defaults; (3) unscheduled draws on debt service reserves reflecting financial difficulties; (4) unscheduled draws on credit enhancements reflecting financial difficulties; (5) substitution of credit or liquidity providers, or their failure to perform; (6) adverse tax opinions or events affecting the status of the Bonds; (7) modifications to rights of holders of the Bonds; (8) Bond calls; (9) defeasances; (10) release, substitution, or sale of property securing repayment of the Bonds; and (11) rating changes. In addition, the City will provide timely notice of any failure by the City to provide information, data, or financial statements in accordance with its agreement described above under “Annual Reports.” The City will provide each notice described in this paragraph to any SID and to either each NRMSIR or the Municipal Securities Rulemaking Board (“MSRB”).

Availability of Information from NRMSIRs and SID

The City has agreed to provide the foregoing information only to NRMSIRs and any SID. The information will be available to holders of the Bonds only if the holders comply with the procedures and pay the charges established by such information vendors or obtain the information through securities brokers who do so.

The Municipal Advisory Council of Texas has been designated by the State as a SID and approved by the SEC. The address of the Municipal Advisory Council is 600 West 8th Street, Austin, Texas, 78701, or Post Office Box 2177, Austin, Texas, 78768-2177 and its telephone number is (512) 476-6947.

The Municipal Advisory Council of Texas has also received SEC approval to operate, and has begun to operate, a “central post office” for information filings made by municipal issuers, such as the City. A municipal issuer may submit its information filings with the central post office, which then transmits such information to the NRMSIRs and the appropriate SID for filing. This central post office can be accessed and utilized at www.DisclosureUSA.org (“DisclosureUSA”). The City may utilize DisclosureUSA for the filing of information relating to the Bonds.

Limitations and Amendments

The City has agreed to update information and to provide notices of material events only as described above. The City has not agreed to provide other information that may be relevant or material to a complete presentation of its financial results of operations, condition, or prospects or agreed to update any information that is provided, except as described above. The City makes no representation or warranty concerning such information or concerning its usefulness to a decision to invest in or sell Bonds at any future date. The City disclaims any contractual or tort liability for damages resulting in whole or in part from any breach of its continuing disclosure agreement or from any statement made pursuant to its agreement, although holders of the Bonds may seek a writ of mandamus to compel the City to comply with its agreement.

This continuing disclosure agreement may be amended by the City from time to time to adapt to changed circumstances that arise from a change in legal requirements, a change in law, or a change in the identity, nature, status, or type of operations of the City, but only if (1) the provisions, as so amended, would have permitted an underwriter to purchase or sell the Bonds in the primary offering described herein in compliance with the Rule, taking into account any amendments or interpretations of the Rule since such offering, as well as such changed circumstances, and (2) either (a) the registered owners of a majority in aggregate principal amount (or any greater amount required by any other provision of the Ordinances that authorize such an amendment) of the outstanding Bonds consent to such amendment or (b) a person that is unaffiliated with the City (such as nationally recognized bond counsel) determined that such amendment will not materially impair the interest of the registered owners and Beneficial Owners of the Bonds. The City may also repeal or amend the provisions of this continuing disclosure agreement if the SEC amends or repeals the applicable provision of the Rule or a court of final jurisdiction enters judgment that such provisions of the Rule are invalid, but only if and to the extent that the provisions of this sentence would not prevent an underwriter from lawfully purchasing or selling Bonds in the primary offering of the Bonds.

Note that the City has, in this Official Statement under the headings “AIRLINES’ RATES AND CHARGES”, “FEDERAL LAW AFFECTING AIRPORT RATES AND CHARGES,” “CERTAIN INVESTMENT CONSIDERATIONS AND RISK FACTORS,” provided investors with information describing circumstances surrounding the airline industry and how such circumstances could potentially affect the Airport’s financial performance. This information is provided, and is accurate, only at this time. The City has undertaken no obligation to update this information as circumstances may warrant and will not include any reference to such material in its required deliveries made pursuant to its continuing disclosure obligations described above.

Compliance With Prior Undertakings

The City has complied in all material respects with all of its previous continuing disclosure agreements in accordance with the Rule.

FORWARD-LOOKING STATEMENTS DISCLAIMER

The statements contained in this Official Statement, including, but not limited to the information under the headings “THE BONDS - Security for the Bonds” and “CERTAIN INVESTMENT CONSIDERATIONS AND RISK FACTORS,” and in any other information provided by the City that are not purely historical are forward-looking statements, including statements regarding the City’s expectations, hopes, intentions, or strategies regarding the future. Readers should not place undue reliance on forward-looking statements. All forward-looking statements included in this Official Statement are based on information available to the City on the date hereof, and the City assumes no obligation to update any such forward-looking statements. The City’s actual results could differ materially from those discussed in such forward-looking statements.

The forward-looking statements included herein are necessarily based on various assumptions and estimates and are inherent subject to various risks and uncertainties, including risks and uncertainties relating to the possible invalidity of the underlying assumptions and estimates and possible changes or developments in social, economic, business, industry, market, legal, regulatory circumstances, and conditions and actions taken or omitted to be taken by third parties, including customers, suppliers, business partners and competitors, and legislative, judicial, and other governmental authorities and officials. Assumptions related to the foregoing involve judgments with respect to, among other things, future economic, competitive, and market conditions of future business decisions, all of which are difficult

or impossible to predict accurately and many of which are beyond the control of the City. Any of such assumptions could be inaccurate and, therefore, there can be no assurance that the forward-looking statements included in this Official Statement will prove to be accurate.

VERIFICATION OF ARITHMETICAL AND MATHEMATICAL COMPUTATIONS

The arithmetical accuracy of certain computations included in the schedules provided by Coastal Securities on behalf of the City was examined by the Verification Agent. Such computations were based solely on assumptions and information supplied by Coastal Securities on behalf of the City. The Verification Agent has restricted its procedures to examining the arithmetical accuracy of certain computations and has not made any study or evaluation of the assumptions and information on which the computations are based, and accordingly, has not expressed an opinion on the data used, the reasonableness of the assumptions, or the achievability of the forecasted outcome. The Verification Agent's report will be relied upon by Bond Counsel in rendering their opinion with respect to the exclusion of interest on the Bonds for federal income tax purposes and with respect to the defeasance of the Refunded Bonds.

CO-FINANCIAL ADVISORS

Coastal Securities and Estrada Hinojosa & Company, Inc. (the "Co-Financial Advisors") are employed by the City in connection with the issuance of the Bonds and, in such capacity, have assisted the City in the preparation of certain documents related thereto. The Co-Financial Advisors' fee for service rendered with respect to the sale of the Bonds is contingent upon the issuance and delivery of the Bonds.

The Co-Financial Advisors have not independently verified any of the information set forth herein. The information contained in this Official Statement has been obtained primarily from the City's records and from other sources which are believed to be reliable, including financial records of the City and other entities which may be subject to interpretation. No guarantee is made by the Co-Financial Advisors as to the accuracy or completeness of any such information. No person, therefore, is entitled to rely upon the participation of the Co-Financial Advisors as an implicit or explicit expression of opinions as to the completeness and accuracy of the information contained in this Official Statement.

UNDERWRITING

The Underwriters, for which Siebert Brandford Shank & Co., LLC is serving as representative, have agreed, subject to certain conditions, to purchase the Bonds from the City at a purchase price of \$18,605,688.55 which represents the par amount of the Bonds, plus a net premium of \$869,923.10 and less an Underwriters' discount of \$114,234.55, plus accrued interest.

The Underwriters' obligations are subject to certain conditions precedent, and they will be obligated to purchase all of the Bonds if any Bonds are purchased. The Bonds may be offered and sold to certain dealers and others at prices lower than such public offering prices, and such public prices may be changed from time to time by the Underwriters.

* * *

AUTHORIZATION OF THE OFFICIAL STATEMENT

This Official Statement has been approved as to form and content and the use thereof in the offering of the Bonds was authorized, ratified, and approved by the City Council on the date of sale, and the Underwriters will be furnished, upon request, at the time of payment for and the delivery of the Bonds, a certified copy of such approval, duly executed by the proper officials of the City.

This Official Statement has been approved by the City Council for distribution in accordance with the provisions of the Rule.

CITY OF SAN ANTONIO, TEXAS

/s/ Phil Hardberger
Mayor

ATTEST:

/s/ Leticia M Vacek
City Clerk

**SCHEDULE I
TABLE OF REFUNDED OBLIGATIONS**

CITY OF SAN ANTONIO, TEXAS

<u>Description of Issue</u>	<u>Amount to be Refunded</u>	<u>Maturities to be Refunded</u>	<u>Interest Rate</u>	<u>Redemption Date</u>	<u>Redemption Price</u>
Airport System Improvement Revenue Bonds, Series 1996	\$ 1,050,000	07/01/2007	5.700%	01/18/2007	101%
	1,125,000	07/01/2008	5.700	01/18/2007	101
	1,175,000	07/01/2009	5.700	01/18/2007	101
	2,425,000	07/01/2010	5.700	01/18/2007	101
	2,575,000	07/01/2011	5.700	01/18/2007	101
	2,700,000	07/01/2012	5.700	01/18/2007	101
	2,875,000	07/01/2013	5.750	01/18/2007	101
	<u>3,800,000</u>	07/01/2014	5.750	01/18/2007	101
TOTAL	<u>\$17,725,000</u>				

APPENDIX A

CITY OF SAN ANTONIO – GENERAL DEMOGRAPHIC AND ECONOMIC INFORMATION

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APPENDIX A

CITY OF SAN ANTONIO GENERAL DEMOGRAPHIC AND ECONOMIC INFORMATION

This Appendix contains a brief discussion of certain economic and demographic characteristics of the City of San Antonio, Texas (the “City” or “San Antonio”) and of the metropolitan area in which the City is located. Although the information in this Appendix has been provided by sources believed to be reliable, no investigation has been made by the City to verify the accuracy or completeness of such information.

Population and Location

The Census 2000, prepared by the U.S. Census Bureau, found a City population of 1,144,646. The City’s Department of Planning estimated the City’s population at 1,306,900 for the calendar year ending December 31, 2005. The U.S. Census Bureau ranks the City as the second largest in the State of Texas and the seventh largest in the United States.

The City is the county seat of Bexar County, which had a population of 1,392,931 according to the Census 2000. The City’s Department of Planning estimated Bexar County’s population at 1,584,800 for the calendar year ending December 31, 2005. The City is located in south central Texas approximately 75 miles south of the state capital in Austin, 140 miles northwest of the Gulf of Mexico, and approximately 150 miles from the U.S./Mexico border cities of Del Rio, Eagle Pass, and Laredo, respectively.

The following table provides, as of April 1 for the years shown, the population of the City, Bexar County, and the San Antonio Metropolitan Statistical Area (“MSA”)¹:

Year	City of San Antonio	Bexar County	San Antonio MSA
1920	161,379	202,096	238,639
1930	231,543	292,533	333,442
1940	253,854	338,176	376,093
1950	408,442	500,460	542,209
1960	587,718	687,151	736,066
1970	654,153	830,460	888,179
1980	786,023	988,971	1,088,881
1990	935,933	1,185,394	1,324,749
2000	1,144,646	1,392,931	1,711,703 ¹

¹ As of June 2003, the United States Office of Management and Budget redefined the San Antonio MSA by increasing the number of counties from four to eight: Atascosa, Bandera, Kendall, and Medina Counties were added to its mainstays of Bexar, Comal, Guadalupe, and Wilson Counties. (The 2000 figure reflects the new 2003 redefined 8-county area.)

Sources: U.S. Census Bureau; City of San Antonio, Department of Planning.

Area and Topography

The area of the City has increased through numerous annexations, and now contains approximately 521 square miles. The topography of San Antonio is generally hilly with heavy black to thin limestone soils. There are numerous streams fed with underground spring water. The average elevation is 788 feet above mean sea level.

Annexation

Through annexation, the City has grown from its original size of 36 square miles to its current area, encompassing 451 square miles (full purpose annexations only) or 521 square miles (both full purpose and limited purpose annexations), and having a fiscal year 2007 total market valuation of \$64.866 billion. The City expects to

continue to utilize the practice of annexation as a future growth and development management tool, as well as an opportunity to enhance the City's fiscal position. Planned annexations by the City are currently under consideration.

At its November 20, 2002 meeting, the City Council annexed, effective December 31, 2002, five areas for inclusion within the City for full purposes, adding 19 square miles of land to the City's total area. At that same meeting, the City Council also annexed, effective January 5, 2003 six areas for limited purposes. Effective August 1, 2004, City Council annexed an additional area for limited purposes south of the Medina River. In addition, effective June 20, 2005, City Council annexed the 4,345-acre Timberwood Park area for limited purposes. The areas annexed for limited purposes account for a total of 70 square miles of land within the City's corporate limits. Limited purpose annexation areas, although included in the total calculation of the City corporate limits, are excluded in the calculation of property values. (See "Limited Purpose Annexation" below).

Limited Purpose Annexation

The City annexed for limited purposes, effective January 5, 2003, six areas south of San Antonio. An additional area south of the Medina River was annexed August 1, 2004 and the Timberwood Park area, immediately east of Camp Bullis, was annexed effective June 20, 2005. Limited purpose annexation allows the City to extend regulatory authority for the limited purposes of applying its planning, zoning, health, and safety ordinances to specified areas. The City may not impose a property tax in such areas until the property is annexed for full purposes, which generally occurs within three years after limited purpose annexation.

As a requirement of Section 43.123, Texas Local Government Code, as amended, the City published a planning study and regulatory plan regarding the proposed limited purpose annexation areas. The planning study addresses projected levels of development in the next ten years with and without annexation of such areas, issues regarding (and the public benefits of) annexation, economic and environmental impact of annexation, and proposed zoning for the specified areas. The regulatory plan outlines development regulations and the respective dates of future, full purpose annexation.

Annexation Plan

In 1999, the Texas Legislature passed Chapter 1167, Acts of the 76th Legislature, Regular Session, 1999 (the "Annexation Act"), changing the manner in which Texas municipalities can annex land. Under the Annexation Act (such requirement now codified at Section 43.052, Texas Local Government Code), municipalities must prepare an annexation plan specifically identifying annexations that may occur beginning on the third anniversary of the date such plan was adopted.

The City Council, at its September 19, 2002 meeting, adopted a three-year annexation plan for the City. At its December 12, 2002 meeting, City Council amended the plan identifying 13 areas for full purpose annexation, as required by Section 43.052 of the Texas Local Government Code, two of these areas were annexed effective December 31, 2005, (along with two other voluntary annexations in December 2005) and two south side limited purpose annexation areas were annexed for full purposes on January 5, 2006. City Council approved an additional amendment to its annexation plan on July 22, 2004, to include the limited purpose annexation south of the Medina River, which is scheduled for full purpose annexation on July 31, 2007.

Form of Government and Administration

The City is a home rule municipality that operates pursuant to the Charter of the City of San Antonio City Charter (the "City Charter"), which was adopted on October 2, 1951 and became effective on January 1, 1952. The City Charter provides for a council-manager form of government. Pursuant to its provisions and subject only to the limitations imposed by the Texas Constitution and the City Charter, all powers of the City are vested in an elective Council (the "City Council") which enacts legislation, adopts budgets, and determines policies. The City Council is comprised of eleven (11) members, with ten (10) members elected from single-member districts, and the Mayor elected at-large. Each member of the City Council serves two (2) year terms, and each member is limited to a maximum of two (2) full terms. The office of the Mayor is considered a separate office. The terms of all members of the City Council currently sitting in office expire on May 31, 2007 or as soon thereafter as a successor is appointed and qualified.

The City Council also appoints a City Manager who executes the laws and administers the government of the City, and serves as the City's chief administrative officer. The City Manager serves at the pleasure of City Council.

City Charter

Since its adoption, the City Charter has been amended on five (5) separate occasions, November 1974, January 1977, May 1991, May 1997, and November 2001. Significant amendments to the City Charter include the amendment passed in May 1991, which limited the service by the Mayor and members of the City Council members to two full terms, each of which is two years in duration. Two (2) separate City Charter review committees sitting in the early and mid-1990's and charged with conducting a comprehensive review of the City Charter resulted in the passage of five propositions, each containing numerous amendments to the City Charter in May 1997. The most recent amendments to the City Charter occurred in 2001 and included, among others, provisions creating the position of an independent City Internal Auditor and granting the City Manager the power to appoint and remove the City Attorney upon the City Council's confirmation and advice, respectively.

Services

The full range of services the City provides to its constituents includes ongoing programs to provide health, welfare, art, cultural, and recreational services; maintenance and construction of streets, highways, drainage, and sanitation systems; public safety through police and fire protection; and urban redevelopment and housing. The City also considers the promotion of convention and tourism and participation in economic development programs high priorities. The funding sources from which these services are provided include ad valorem, sales, and hotel/motel tax receipts, federal and state grants, user fees, bond proceeds, tax increment financing, and other sources.

In addition to the above described general government services, the City provides services financed by user fees set at levels adequate to provide coverage for operating expenses and the payment of outstanding debt. These services include airport, parking, storm water, and environmental services.

Electric and gas services to the San Antonio area are provided by City Public Service ("CPS"), an electric and gas utility owned by the City that maintains and operates certain utilities infrastructure. This infrastructure includes a 19 generating unit electric system and the gas system that serves the San Antonio area. CPS operations and debt service requirements for capital improvements are paid from revenues received from charges to its customers. CPS is obligated to transfer a portion of its revenues to the City. CPS revenue transfers to the City for the City's fiscal year ending September 30, 2005 were \$213,384,307.

Water, wastewater, recycled water, steam, and chilled water services are provided by the San Antonio Water System ("SAWS"), another City-owned and operated utility. In addition to these services, SAWS contracted with the City to provide certain storm water services thereto and it manages and develops water resources in and around the San Antonio region. SAWS is in its 14th year as a separate, consolidated entity that addresses the City's water-related issues in a coordinated and unified manner. SAWS operations and debt service requirements for capital improvements are paid from revenues received from charges to its customers. SAWS is obligated to transfer a portion of its revenues to the City. SAWS revenue transfers to the City for the City's fiscal year ended September 30, 2005 were \$8,390,366.

Economic Factors

The City supports a favorable business environment and economic diversification which is represented by various industries, including domestic and international trade, convention and tourism, medicine and health care, government employment, agribusiness, manufacturing, financial services, telecommunications, telemarketing, insurance, and oil and gas refining. Support for these economic activities is demonstrated by the City's commitment to its on-going infrastructure improvements and development and its dedicated work force. Total employment in the San Antonio MSA for August 2006 was 881,940, which is 20,013 or 2.33% more jobs than the August 2005 total of 861,927. Services, trade, and government represent the largest employment sectors in the San Antonio MSA.

Finance (including insurance), healthcare and bioscience, tourism, and the military represent the largest industries in San Antonio.

Finance Industry

According to a study conducted by the Finance San Antonio Ad Hoc Committee, the finance industry is San Antonio's largest economic generator with an annual economic impact of \$20.5 billion in 2004. The industry employs 50,469 people to whom it pays an average wage of \$52,612, considerably higher than the average wage of \$33,911. Total wages paid in the industry amounted to \$2.66 billion in 2004. As a percent of total employment, the finance industry in San Antonio is the largest of any major metropolitan area in Texas. Compared to the growth in wages and employment in San Antonio overall, the finance industry experienced higher levels of average annual growth in these areas since 2001. Average annual growth in total wages paid by the finance industry for years 2001 through 2004 was 4.5%, compared to 4% for all industries. Average annual growth in employment in the finance industry over this same time period was 2.18%, compared to 0.36% for all other industries.

The largest sector in this industry is insurance. While this sector is led by USAA, San Antonio is home to several other insurance headquarters such as Argonaut Group, Catholic Life, GPM Life, as well as being the home to many regional operations centers for many health care insurers. Insurers with substantial regional operations centers in San Antonio include Caremark, United Health, and Pacificare.

The second largest sector in this industry is banking. Like insurance, San Antonio is also the home of many banking headquarters and regional operation centers such as Frost Bank, Broadway Bank, and USAA Bank. Companies with large regional operations centers in San Antonio include World Savings, Chase, and Citicorp. Each of these companies has experienced substantial growth since arriving in San Antonio, and they continue to grow today. In addition to this growth, Washington Mutual has just opened a regional operations center that will result in the creation of 2,000 to 5,000 jobs over the next several years.

Healthcare & Bioscience Industry

The healthcare and bioscience industry remains the largest industries in the San Antonio economy. The industry is diversified, with related industries such as research, pharmaceuticals, and manufacturing contributing approximately the same economic impact as health services. According to the *San Antonio's Healthcare and Bioscience Industry Economic Impact Study* commissioned by the Greater San Antonio Chamber of Commerce, the total economic impact from this industry sector totaled approximately \$13.7 billion in 2004. The industry provided more than 109,000 jobs, or approximately 14.6 percent of the City's total employment. The healthcare and bioscience industry's annual payroll in 2004 approached \$4.2 billion. The 2004 average annual wage of San Antonio workers was \$33,911, compared to \$38,531 for healthcare and bioscience employees. These 2004 economic impact figures represent growth of 4 percent over the previous year, or approximately \$800 thousand.

Health Care. The 900-acre South Texas Medical Center (the "Medical Center") has ten major hospitals and nearly 80 clinics, professional buildings, and health agencies with combined budgets of over \$2.5 billion as of January 2005. Approximately 26,757 Medical Center employees provided care for over 3.92 million outpatients and over 102,000 inpatients. Physical plant values, not adjusted for inflation, representing the original investments in physical facilities and equipment (less depreciation) represents approximately \$1.854 billion, which is a \$120 million increase in 2004 over the previous year. The Medical Center has about 300 acres of undeveloped land still available for expansion. Capital projects already in progress total \$65 million. Capital projects planned for the years 2006 through 2010 will add an additional estimated \$152 million to present physical plant and equipment values.

Central to the Medical Center is The University of Texas Health Science Center at San Antonio (the "UT Health Science Center") with its five professional schools awarding more than 50 degrees and certificates, including Doctor of Medicine, Doctor of Dental Surgery, and Doctor of Philosophy in nursing, allied sciences, and other fields. The UT Health Science Center oversees the new, federally-funded Regional Academic Health Center in the Rio Grande Valley with facilities in Harlingen, McAllen, Brownsville, and Edinburg. An extension campus is under construction in Laredo, Texas.

There are numerous other medical facilities outside the boundaries of the Medical Center, including 25 short-term general hospitals, two children's psychiatric hospitals, and two state hospitals. There are three Department of Defense hospitals, one of which is located in the Medical Center (as hereinafter described).

Military Health Care. San Antonio has three major military hospitals, each of which has positively impacted the City for decades. Brooke Army Medical Center ("BAMC") conducts treatment and research in a new, 1.5 million square foot facility at Fort Sam Houston United States Army Base, providing health care to nearly 600,000 military personnel and their families. BAMC is a level-one trauma center (the only one in the United States Army medical care system) and contains the world-renowned Institute of Surgical Research Burn Center. BAMC also conducts bone marrow transplants in addition to more than 600 ongoing research studies.

Wilford Hall Medical Center ("Wilford Hall") is the largest medical facility of the United States Air Force. In addition to providing health care to military personnel and their families, Wilford Hall is also a level-one trauma center (the only one in the United States Air Force medical care system) that handles emergency medical care for approximately one-fourth of the City's emergency patients. Wilford Hall provides medical education for the majority of its physician and dental specialists and other health professionals, conducts clinical investigations, and offers bone marrow and organ transplantation.

Audie L. Murphy Memorial Veterans Hospital, located in the Medical Center, is an acute care facility and supports a nursing home, the Spinal Cord Injury Center, an ambulatory care program, the Audie L. Murphy Research Services (which is dedicated to medical investigations), and the new Frank Tejeda Veterans Administration Outpatient Clinic (which serves veterans located throughout South Texas).

The two military medical care facilities and the Veterans Hospital partner in a variety of ways, including clinical research and the provision of medical care to military veterans. This partnership is unique and represents a valuable resource to San Antonio and the nation.

Biomedical Research and Development. Research and development are important areas that strengthen San Antonio's position as an innovator in the biomedical field, with total research economic impact exceeding \$1.005 billion annually.

The Texas Research Park (the "Park") is the site for the University of Texas Institute of Biotechnology/Department of Molecular Medicine, the Cancer Therapy and Research Center ("CTRC"), and CTCRC's Research Center's Institute for Drug Development, The Southwest Oncology Group, and dozens of new biotechnology-related companies, whose work involves various stages of the very complicated drug development process. The Park has over \$100 million invested in its facilities and equipment and generates more than \$200 million in economic activity for the City each year. The Park is owned and operated by the Texas Research and Technology Foundation, whose mission includes building a world-class center for life-science research and medical education and promoting economic development through job creation.

The Southwest Foundation for Biomedical Research, which conducts fundamental and applied research in the medical sciences, is one of the largest independent, non-profit, biomedical research institutions in the United States, and is internationally renowned. The Southwest Foundation for Biomedical Research has a full time staff of 72 doctoral level employees, a technical staff of 115, and an administrative and supporting staff of 201 persons. Research departments include Departments of Genetics, Physiology and Medicine, Virology and Immunology, and Organic and Biological Chemistry. The Department of Laboratory Animal Medicine maintains the animal care facilities. The Foundation is also home to one of the few Biosafety Level 4 labs in the country, and its Genomics Computing is the world's largest computer cluster devoted to statistical genetic analysis.

The UT Health Science Center has been a major bioscience research engine since its inception, with strong research groups in cancer, cancer prevention, diabetes, drug development, geriatrics, growth factor and molecular genetics, heart disease, stroke prevention, and many other fields. One of its latest achievements is the establishment of the Children's Cancer Research Center, endowed with \$200 million from the State of Texas's tobacco settlement. The UT Health Science Center, along with the CTCRC, forms the San Antonio Cancer Institute, a National Cancer Institute-designated Comprehensive Cancer Center.

UTSA houses the Cajal Neuroscience Research Center, which is funded by \$11 million in ongoing grants and is tasked with training students in research skills while they perform basic neuroscience research on subjects such as aging and Alzheimer's disease. UTSA is also the recipient of more than \$35 million for its new School of Bioengineering.

A number of highly successful private corporations, such as Mission Pharmacal, DPT Laboratories, Ltd., and Genzyme Oncology, Inc., operate their own research and development groups and act as guideposts for numerous biotech startups, bringing new dollars into the area's economy. A notable example of the results of these firms' research and development is Genzyme Oncology, Inc., which has developed eight of the last 11 cancer drugs approved for general use by the Federal Drug Administration.

Hospitality Industry

The City's diversified economy includes a significant sector relating to the hospitality industry. A recent study by the Greater San Antonio Chamber of Commerce found that in 2004 the hospitality industry had an economic impact of nearly \$8.7 billion. The estimated annual payroll for the industry in 2004 was \$1.58 billion, and the industry employed over 94,000. The updated economic impact study is tentatively scheduled in 2008.

In 2005, the City's overall performance for hotel occupancy increased by 7.1%, revenue per available room ("RevPAR") increased by 13.0%, and total room nights sold in the destination increased by 8.4%.

Tourism. During 2004, San Antonio attracted over 21.3 million visitors with direct spending across all industries of \$4.3 billion and ranked tenth among U.S. destinations for overnight leisure travel, according to the National Performance Monitor survey conducted by D.K. Shifflet & Associates. This information is updated on a biennial basis with the next release scheduled for August 2007. The list of attractions in the San Antonio area includes, among many others, the Alamo, and other sites of historic significance, the River Walk, two major theme parks (SeaWorld of Texas and Six Flags Fiesta Texas), and the professional basketball team, the San Antonio Spurs.

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Conventions. San Antonio is one of the top convention cities in the country. The City is proactive in attracting convention business through its management practices and marketing efforts. The following table shows both overall city performance as well as convention activity booked by the San Antonio Convention & Visitors Bureau for the years indicated:

Fiscal Year Ended 9/30	Hotel Occupancy ¹	Hotel RevPAR ¹	Room Nights Sold ¹	Convention Attendance ²	Convention Room Nights ²	Convention Delegate Expenditures (\$ Millions) ^{2, 3}
1996	65.1%	\$49.95	5,515,798	486,383	725,395	\$398.3
1997	63.0%	\$50.21	5,642,517	417,492	670,039	\$341.9
1998	64.8%	\$53.14	6,011,449	445,151	724,882	\$401.0
1999	64.3%	\$53.18	6,151,548	406,539	678,014	\$366.2
2000	64.7%	\$55.33	6,550,338	389,448	696,215	\$350.8
2001	62.7%	\$54.09	6,487,396	419,970	712,189	\$378.3
2002	63.9%	\$55.41	6,741,457	482,770	703,200	\$434.9
2003	63.9%	\$53.26	6,906,013	430,983	615,576	\$388.3
2004	64.6%	\$55.11	7,022,270	491,257	621,592	\$510.5
2005	69.1%	\$62.30	7,615,082	495,127	730,899	\$514.5

¹ Data obtained from Smith Travel Research based on hotels in San Antonio as of July 27, 2006.

² Reflects only those conventions booked by the Convention and Visitors Bureau.

³ For the years of 1996 and 1997, the estimated dollar value is calculated in accordance with a 1993 Deloitte & Touche LLP study for the International Association of Convention and Visitor Bureaus ("IACVB") which reflected the average expenditure of \$818.82 per convention and trade show delegate. Beginning in 1998, the estimated dollar value is calculated in accordance with the 1998 IACVB Foundation Convention Income Survey Report conducted by Deloitte & Touche LLP, which reflected the average expenditure of \$900.89 per convention and trade show delegate. Calendar year 2004 is based on an average expenditure of \$1,030.20 per convention and trade show delegate, according to a Veris Consulting, LLC study for the IACVB.

Military Industry

The military represents a principal component of the City's economy providing an annual economic impact for the City of over \$5 billion. Three major military installations are currently located in Bexar County, including Lackland Air Force Base ("Lackland AFB"), Fort Sam Houston Army Base ("Fort Sam"), and Randolph Air Force Base ("Randolph AFB"). In addition, the property of Brooks Air Force Base ("Brooks AFB"), a fourth major military installation, was transferred from the United States Air Force (the "Air Force") to the City-created Brooks Development Authority ("BDA") in 2002, as part of the Brooks City-Base Project ("Brooks City-Base"). Furthermore, the military is still leasing over two million square feet of space at KellyUSA, which is the former Kelly Air Force Base that was closed in 2001.

KellyUSA. On July 13, 2001, Kelly Air Force Base ("Kelly AFB") officially closed and the land and facilities were transferred to the Greater Kelly Development Authority ("GKDA"), a City Council-created organization responsible for overseeing the redevelopment of the base into a business and industrial park. The new business park, known as KellyUSA, is focused on becoming the Port of San Antonio by: (1) establishing international air cargo operations; (2) developing a rail port for direct international rail operations including inland port distribution with the Port of Corpus Christi; (3) expanding aviation maintenance, repair, and overhaul ("MRO") operations into a renowned international center of excellence for MRO.

As of December 2005, there were over 63 tenants employing over 12,469 people with an average salary of over \$38,000 and a total economic impact of \$2.76 billion per year. Major commercial employers at KellyUSA include Boeing, Lockheed Martin, General Electric, General Dynamics, Standard Aero, Pratt & Whitney, Chromalloy, Gore Design Completions, and EG&G.

With 95% of the marketable 8.2 million square feet leased, GKDA is now focused on development of new Class A facilities leveraging public and private investment to create more jobs for San Antonio. In 2005, a total of 514,400 square feet of new hangar, distribution, and flex/office facilities were constructed at KellyUSA. GKDA's

development plan forecasts \$336 million of new construction for buildings and infrastructure over the next 5 years. KellyUSA's economic impact to San Antonio is projected to increase to over \$4.6 billion per year upon full build-out.

Brooks City-Base. Brooks City-Base continues to draw private business investment, however, the military missions will be relocated over the next three to five years as a result of the 2005 Base Realignment and Closure (see "BRAC" herein) recommendations. The City is several years ahead in redevelopment over the other military installations across the United States facing the same relocations and closures from the BRAC. Despite the BRAC decision, Brooks City-Base is continuing its goal of sustainability by creating a Tax Increment Reinvestment Zone that encompasses the area inside and outside the Brooks City-Base as another tool to assist in its development. As a timeline is determined for the departure of Air Force missions, the BDA will have a better idea how best to redevelop the approximately 2 million square feet of current total space including lab, office and light industrial space.

Currently, there are over \$170 million worth of projects planned for or are already underway. Some of these project highlights include:

In 2005, the BDA and a local pharmaceutical company, Dermatological Products of Texas ("DPT") Laboratories, approved an eighteen-year build-to-suit lease agreement for a combination research and development warehouse and production facility of nearly a quarter-million square feet at Brook-City Base. The project involves a capital investment of \$24 million and construction is underway on the two new major buildings located at Brooks City-Base.

Vanguard Health Systems, Inc. and its affiliate Baptist Health System ("BHS") announced in 2005 that BHS has signed a letter of intent to acquire land to relocate Southeast Baptist Hospital to Brooks City-Base. The new hospital will initially be sized for 175 beds, but ultimately, the hospital could grow to more than 400 beds. The new hospital will bring 700 to 800 jobs to the south side of San Antonio and represents a significant economic investment in the community. Groundbreaking is expected to occur in mid 2006 with a grand opening slated for late 2007 or early 2008. Ultimately, the hospital will be part of a medical campus with one medical office building being constructed concurrently with the hospital and six additional buildings constructed under a phased timeline.

A \$24.5 million Emergency Operations Center (the "EOC") is to be constructed at Brooks City-Base. The EOC, which will be financed through City and Bexar County proposed bond funds, will be the anchor of the planned Emergency Preparedness Institute, and will be a campus of City, County, Regional, State and Federal departments and/or personnel. The EOC is anticipated to be operational by December 2007.

The San Antonio Metropolitan Health District ("SAMHD") has completed renovation of a Brooks City-Base facility to establish a Biosafety Level 3 ("BSL3") Laboratory. SAMHD plans to institute additional public health capabilities at Brooks City-Base and is investigating plans to move the majority of its downtown resources to the BSL3 Laboratory at Brooks City-Base.

The Texas State Board of Education approved the charter school application filed by Somerset Academy in collaboration with the Brooks City-Base Foundation and the BDA, allowing for the development of a charter school at Brooks City-Base. Construction will be underway soon with classes set to start in September 2006. The school's curriculum will focus on science and engineering, providing students with a unique opportunity to learn and participate in the cutting-edge Air Force programs found at Brooks City-Base and throughout San Antonio.

Fort Sam and Lackland AFB. Fort Sam is engaged in military-community partnership initiatives to help reduce infrastructure costs and pursue asset management opportunities using military facilities. In April 2000, the United States Army (the "Army") entered into a partnership with the private organization, Fort Sam Houston Redevelopment Partners, Ltd. ("FSHRP"), for the redevelopment of the former Brooke Army Medical Center and two other buildings at Fort Sam. These three buildings, totaling about 500,000 square feet in space and located in a designated historic district, had been vacant for some time and were in a deteriorating condition. On June 21, 2001, FSHRP signed a 50-year lease with the Army to redevelop and lease these three properties to commercial tenants.

In September 2003, the Army relocated Army South Headquarters from Puerto Rico to Fort Sam, bringing approximately 500 new jobs to San Antonio with an annual economic impact of approximately \$200 million. The Army negotiated a lease with the FSHRP to locate United States Army South and the Southwest Region Installation Management Agency in the newly renovated historic facilities in the summer of 2004. The continued success of this unique public-private partnership at Fort Sam is critical to assisting the Army in reducing infrastructure support costs, preserving historical assets, promoting economic development opportunities, and generating net cash flow for both the Army and FSHRP.

This project supports the City's economic development strategy to promote development in targeted areas of the City, leverage military installation economic assets to create jobs, and assist our military installations in reducing base support operating costs. The Army intends to extend the public-private partnership initiative to include other properties at Fort Sam currently available for redevelopment.

Base Realignment and Closure ("BRAC"). On November 8, 2005, the recommendations of the BRAC Commission became law. As a result of BRAC, the San Antonio area will benefit from a net gain of about 3,600 jobs over the next three to five years. In addition, transformation is ongoing throughout the military services resulting in the reorganization of many military missions and units. For example, at Fort Sam, the Army transformation actions are expected to create an additional 4,000 jobs over the next few years in addition to the growth from BRAC discussed below. Furthermore, the Texas Cryptologic Center has announced an expansion of its activities in San Antonio and will be adding about 1,500 jobs over the next two years.

Key elements of BRAC include the creation of a the United States Department of Defense ("DoD") Regional Medical Center at the new BAMC and the establishment of Fort Sam Houston as the home for all DoD enlisted medical training. BAMC will be one of only two such DoD Regional Medical Centers in the country and will merge with the Wilford Hall at Lackland AFB. While the Wilford Hall facility at Lackland will close, the DoD intends to build a new 450,000 square foot medical care clinic at Lackland. In addition, a number of Army Agency Headquarters will also be relocating to Fort Sam from other bases around the country. As these changes occur over the next three to six years, Fort Sam Houston will grow by over 13,000 jobs to about 40,000. Based on the planned changes at Fort Sam and Lackland AFB, the community is also expecting to benefit from over \$2 billion in new construction and renovation of facilities at both bases. Finally, the recommended BRAC enhancements to military medical care training and capacity will also greatly strengthen and grow the currently existing partnerships between the military and community institutions. These will facilitate continued growth in the community's number one targeted industry of bioscience and healthcare.

Defense Transformation Institute ("DTI"). DTI is a non-profit entity established by the Texas Research and Technology Foundation in partnership with the City. DTI's mission is to leverage the assets at active duty military installations to create value for the military and the community. These military assets can include land, facilities, education, technology, research, and training. DTI is also prepared to act as the community's lead agency for partnering with the military to help plan, coordinate, implement, and accelerate the results of BRAC 2005 to the benefit of the military and the community. DTI is also partnering with the State to conduct workshops on how communities can effectively partner with their military counterparts to achieve mutual benefit.

Other Major Industries

Aerospace. The aerospace industry's annual economic impact to the City is about \$3.3 billion. This industry provides some 9,535 jobs, with employees earning total annual wages of over \$406 million. The aerospace industry continues to expand as the City leverages its key aerospace assets, which include San Antonio International Airport, Stinson Municipal Airport, KellyUSA, Randolph AFB and Lackland AFB, and training institutions. Many of the major aerospace industry participants have significant operations in San Antonio, such as Boeing, Lockheed Martin, General Electric, Pratt & Whitney, Raytheon, Cessna, San Antonio Aerospace – a division of Singapore Technologies, Southwest Airlines, American Airlines, Delta and Continental, FedEx, UPS, and others. The industry in San Antonio is much diversified with continued growth in air passenger service, air cargo, MRO, and general aviation.

Aerospace Research and Development. In May 2005, the National Sustainment Technology Center (NSTC) opened in San Antonio to research and develop solutions to address the challenges and requirements faced

by the DoD in the maintenance of aging weapon systems. The NSTC falls under the Defense Sustainment Consortium (“DSC”) which is a collaboration of DoD and industry stakeholders involved in the acquisition and support for DoD weapon systems. The NSTC will conduct funded pilot projects involving DSC members, academia, and government partners to produce innovative solutions for unique problems associated with aging weapon systems. The NSTC will also promote technology transfer from small business to DoD customers and defense contractors. By having the NSTC in San Antonio, local businesses, educational institutions, and other public/private entities can collaborate to compete for these research and development opportunities.

San Antonio Technology Accelerator Initiative. San Antonio Technology Accelerator Initiative (“SATAI”) is a targeted economic development initiative focused on developing an advanced technology economy in the San Antonio region. SATAI’s mission is to accelerate the regional technological economy through providing hands-on development of advanced technology start-up companies and assisting established companies in accessing technology-based solutions through Enterprise Services. SATAI recently become the home of the South Texas Regional Commercialization and Innovation Center (“STRCIC”). The STRCIC was established in response to the creation of the Emerging Technology Fund by the State of Texas. Its purpose is to review funding requests submitted by technology startup companies who are seeking funding from the Emerging Technology Fund.

In this past legislative session, the State of Texas (the “State”) created the \$200 million Emerging Technology Fund (“ETF”). The ETF is to be used to help foster the development of the technology industries in San Antonio by providing another source of financial capital to entrepreneurs, providing matching grants for research, and allocating funds to be used to acquire research superiority at colleges and universities throughout the state. In order to participate in the ETF, the Bexar County region is establishing a Regional Center of Innovation and Commercialization (“RCIC”), as required by law. The RCIC will review potential commercialization opportunities presented by local entrepreneurs and make recommendations for possible funding to the Texas Emerging Technology Committee. The State has recognized the SATAI to serve as the RCIC for the San Antonio region. In the first two rounds in which money was granted, three San Antonio companies received a total of \$2.8 million and UTSA received \$3.5 million to help attract world-class information security professors and researchers.

In May 2005, the community also formed the Defense Technology Cluster (the “Cluster”) in partnership with the SATAI. The Cluster is a collaboration of local companies currently doing business with the Department of Defense and/or the Department of Homeland Security. Through this collaboration, the Cluster expects to attract more defense technology work to San Antonio, create an awareness of the technical capabilities of local firms, and promote the growth and expansion of defense technology companies in the community. The Cluster seeks to become the recognized source for information and resources on the talent and capabilities of firms in the San Antonio region available to support defense technology requirements.

Applied Research & Development. The Southwest Research Institute is one of the original and largest independent, nonprofit, applied engineering and physical sciences research and development organizations in the United States, serving industries and governments around the world in the engineering and physical sciences. Southwest Research Institute has contracts with the Federal Aviation Administration, General Electric, Pratt & Whitney, and other organizations to conduct research on many aspects of aviation, including testing synthetic jet fuel, developing software to assist with jet engine design, and testing turbine safety and materials stability. Southwest Research Institute occupies 1,200 acres and provides nearly two million square feet of laboratories, test facilities, workshops, and offices for more than 2,700 scientists, engineers, and support personnel.

Telecommunications Industry. San Antonio became the headquarters for AT&T, Inc. (“AT&T”) after SBC Communications, Inc. (“SBC”) acquired the New Jersey-based company for \$16 billion and took its name in 2005. The recently completed merger created one of the largest telecommunications and networking companies in the world and the largest national phone service provider. According to a published report, this will result in more than 100 AT&T employees relocating to San Antonio, including senior executives. The newly merged AT&T has approximately 189,950 employees worldwide as of December 2005.

Information Technology. The Information Technology (“IT”) industry is one of the fastest- growing sectors of the local economy. A study conducted in 2001, cites that the IT industry in San Antonio registered an overall economic impact of approximately \$3.4 billion which represents about seven percent of the San Antonio economy. The annual payroll among the IT industry’s estimated 11,500 employees totals approximately \$500

million. The IT industry is particularly strong in the areas of information security and government contracting. The Center for Infrastructure Assurance and Security at the University of Texas at San Antonio is one of the leading research and education institutions in the area of information security in the country. In 2005, the United States National Security Agency (the “NSA”) re-designated the University of Texas at San Antonio a National Center of Excellence in Information Assurance for three academic years. San Antonio is also home to the Air Intelligence Agency, which is the premier IT agency for the Air Force and the DoD. Adding to the growth of this industry, the Texas Cryptologic Center recently announced they are investing \$300 million in a new facility and adding at least 1,500 new jobs over the next few years in San Antonio.

Manufacturing Industry. The manufacturing industry of the City’s economy has seen significant growth over the past two years, in large part due to the construction of the new Toyota Motor Manufacturing (“Toyota”) facility and the development of the Toyota Supplier Park at its manufacturing site. Toyota will invest over \$850 million in this manufacturing facility, located on 2,000 acres in south San Antonio, and at full production, the facility will produce 200,000 full-size Tundra trucks. At full operations, the payroll for the 2,000 workers at the facility will total between \$90 and \$100 million. The Toyota Supplier Park has attracted 21 Tier-One supplier companies resulting in an additional capital investment of over \$300 million and 2,100 additional automotive manufacturing jobs.

In order to support the growth of the manufacturing sector, the Manufacturing Technology Academy was created in 2004. At this Academy, high school students learn many skills applicable to a variety of manufacturers, including manual and automated welding, machining, safety techniques, and total quality management.

Creative Industry. The creative industry in San Antonio registers a \$1.2 billion economic impact, employs 11,888 people, and pays annual wages of \$319 million. This industry consists of the following sectors, with economic impact in parentheses: performing arts (\$475.3 million), design, and advertising (\$401.1 million), museums and collections (\$233.7 million), visual arts and photography (\$84.0 million), and fine arts schools (\$22.1 million). If the printing, publishing, and broadcasting sectors were included, the economic impact would be \$3.5 billion. Recognizing the overall impact of this industry, *The Cultural Collaborative: A Plan for San Antonio’s Creative Economy*, was created and a strategic plan was developed to provide focus and initiative for the future of this industry.

Sources: The Greater San Antonio Chamber of Commerce; San Antonio Medical Foundation; City of San Antonio, Department of Economic Development and Convention and Visitors Bureau.

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Growth Indices

San Antonio Electric and Gas Customers

<u>For the Month of December</u>	<u>Electric Customers</u>	<u>Gas Customers</u>
1996	528,302	299,140
1997	538,729	301,044
1998	548,468	301,842
1999	560,628	302,991
2000	575,461	305,181
2001	589,426	305,702
2002	594,945	306,503
2003	602,185	306,591
2004	617,261	308,681
2005	638,344	310,699

Source: CPS.

San Antonio Water System Average Customers per Fiscal Year

<u>Fiscal Year Ended May 31</u> ^{1, 2}	<u>Water Customers</u> ³
1996	269,405
1997	273,276
1998	270,897
1999	279,210
2000	285,887
2001	292,136
2002	298,215
2003	303,917
2004	311,554
2005	323,149

¹ On April 3, 2001, the SAWS Board of Trustees approved the changing of SAWS' fiscal year from a year-end of May 31 to December 31.

² Beginning in year 2001, for the 12 months ending December 31.

³ Excluding SAWS irrigation customers.

Source: SAWS.

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Construction Activity

Set forth below is a table showing building permits issued for construction within the City at December 31 for the years indicated:

Calendar Year	Residential Single Family		Residential Multi-Family ¹		Other ²	
	Permits	Valuation	Permits	Valuation	Permits	Valuation
1996	4,306	\$ 261,540,367	171	\$ 64,282,630	9,055	\$ 578,225,607
1997	4,240	257,052,585	155	42,859,473	8,170	717,988,779
1998	5,630	363,747,169	85	23,194,475	8,193	892,766,648
1999	5,771	398,432,375	404	157,702,704	9,870	911,543,958
2000	5,494	383,084,509	201	81,682,787	10,781	957,808,435
2001	6,132	426,766,091	449	142,506,920	12,732	1,217,217,803
2002	6,347	435,090,131	246	101,680,895	14,326	833,144,271
2003	6,771	521,090,684	141	2,738,551	13,813	1,041,363,980
2004	7,434	825,787,434	206	7,044,283	14,695	1,389,950,935
2005	8,207	943,804,795	347	5,221,672	20,126	1,772,959,286

¹ Includes two-family duplex projects.

² Includes commercial building permits, commercial additions, improvements, extensions, and certain residential improvements.
Source: City of San Antonio, Department of Development Services.

Total Municipal Sales Tax Collections – Ten Largest Texas Cities

	Calendar Year				
	2005	2004	2003	2002	2001
Amarillo	\$ 50,524,792	\$ 48,155,445	\$ 44,581,868	\$ 44,201,183	\$ 43,357,043
Arlington	61,983,154	49,344,578	46,483,314	42,493,256	65,948,096
Austin	118,853,520	112,515,478	105,044,871	110,208,923	117,393,240
Dallas	199,585,955	192,972,586	184,263,151	192,542,321	210,130,838
El Paso	54,217,823	51,461,838	48,949,656	47,465,776	46,876,210
Fort Worth	83,754,760	76,202,528	72,772,964	72,632,487	72,975,421
Houston	380,871,932	355,616,488	325,284,697	334,122,179	337,540,694
Irving	41,573,304	37,719,779	36,584,559	38,810,594	43,188,105
Plano	53,036,662	49,453,998	46,876,867	45,309,249	47,327,003
SAN ANTONIO	161,951,337	157,284,972	152,360,840	153,207,656	151,422,401

Source: State of Texas, Comptroller's Office.

Education

There are 15 independent school districts within Bexar County with a combined enrollment of 281,371 encompassing in the aggregate 41 high schools, 70 middle/junior high schools, and 247 elementary schools as of October 2005. There are an additional 25 charter school districts with 53 open enrollment charter schools at all grade levels. In addition, Bexar County has 94 accredited private and parochial schools at all education levels. Generally, students attend school in the districts in which they reside. There is currently no busing between school districts in effect.

The six largest accredited and degree-granting universities, which include a medical school, a dental school, and a law school, and four public community colleges, had combined enrollments of 96,943 for fall 2005.

Source: Texas Education Agency.

Employment Statistics

The following table shows current nonagricultural employment estimates by industry in the San Antonio MSA for the period of August 2006, as compared to the prior periods of July 2006 and August 2005.

Employment by Industry

<u>San Antonio MSA¹</u>	<u>August 2006</u>	<u>July 2006</u>	<u>August 2005</u>
Natural Resources, Mining and Construction	51,300	51,000	48,500
Manufacturing	46,900	47,300	46,100
Trade, Transportation, and Utilities	140,100	139,100	140,700
Information	20,300	20,400	20,800
Financial Activities	63,500	63,400	63,000
Professional and Business Services	102,300	103,000	97,300
Educational and Health Services	108,900	107,600	105,800
Leisure and Hospitality	96,800	97,400	94,300
Other Services	28,100	28,100	27,800
Government	<u>140,200</u>	<u>138,500</u>	<u>138,700</u>
Total Nonagricultural	798,400	795,800	783,000

The following table shows civilian labor force estimates, the number of persons employed, the number of persons unemployed, and the unemployment rate in the San Antonio MSA, Texas, and the United States for the period of August 2006, as compared to the prior periods of July 2006 and August 2005.

Unemployment Information (all estimates are in thousands)

<u>San Antonio MSA¹</u>	<u>August 2006</u>	<u>July 2006</u>	<u>August 2005</u>
Civilian Labor Force	926.5	926.5	906.3
Number of Employed	881.9	877.8	861.9
Number of Unemployed	44.6	48.7	44.4
Unemployment Rate %	4.8	5.3	4.9
<u>Texas (Actual)¹</u>	<u>August 2006</u>	<u>July 2006</u>	<u>August 2005</u>
Civilian Labor Force	11,538.6	11,579.5	11,264.0
Number of Employed	10,949.9	10,945.0	10,676.4
Number of Unemployed	588.7	634.5	587.6
Unemployment Rate %	5.1	5.5	5.2
<u>United States (Actual)²</u>	<u>August 2006</u>	<u>July 2006</u>	<u>August 2005</u>
Civilian Labor Force	152,465.0	153,208.0	150,469.0
Number of Employed	145,379.0	145,606.0	143,142.0
Number of Unemployed	7,086.0	7,602.0	7,327.0
Unemployment Rate %	4.6	5.0	4.9

¹ Based on Labor Market Information Department, Texas Workforce Commission (model-based methodology).

² Based on Bureau of Labor Statistics, U.S. Department of Labor (Current Population Survey).

**Employers with 500 or More Employees in the San Antonio Metropolitan Area
(Includes Bexar, Comal, Guadalupe, and Wilson Counties)¹**

Firm	Product/Service	Firm	Product/Service
Construction:			
CCC Group, Inc.	Industrial Contractor	Urban Concrete Contractors, Ltd.	Exterior Concrete Contractor
Design Electric	Electrical Contractor	Zachry Group	Industrial General Contracting
Finance, Insurance, & Real Estate:			
American Funds	Mutual Funds & Investments	San Antonio Federal Credit Union	Credit Union/Financial Services
Argonaut Group	Insurance	Security Service Federal Credit Union	Credit Union/Financial Services
Bank of America - San Antonio	Commercial & Individual Banking	The Hartford	Personal Insurance
Frost National Bank	Financial Services & Insurance	The Lynd Company	Real Estate Brokerage
Humana	Medical Insurance Plans	USAA	Insurance/Financial Services
JP Morgan Chase Bank	Commercial & Individual Banking	Washington Mutual Bank	Banking, Financial Services
Pacificare	Medical Insurance Plans	Wells Fargo Bank	Banking, Financial Services
Randolph-Brooks FCU	Credit Union/ Financial Services	World Savings	Banking, Financial Services
SWBC	Insurance, Residential Mortgages		
Government:			
Bexar County	County Government	Randolph Air Force Base	Military Installation
Brooks City-Base	Military Installation	San Antonio Housing Authority	Public Housing Assistance
City of San Antonio	Municipal Government	Texas Department of Transportation	Highway Construction/Maint.
Education Service Center Region 20	State Education Service Agency	Texas Dept. of Family & Child Protective Services	State Social Services
Fort Sam Houston-US Army Base	Military Installation	Texas Dept. of Health & Human Services	State Social Services
Guadalupe County	County Government	VIA Metropolitan Transit	Urban Public Transportation
Lackland Air Force Base	Military Installation		
Manufacturing:			
Alamo Concrete Products	Concrete Products	Miller Curtain Company	Curtains, Draperies, & Bedspreads
Cardell Cabinetry	Cabinetry	Motorola	Electronics
Clarke American	Check Printing	SAS Shoemakers	Shoes
Coca-Cola Bottling Co. of the SW	Soft Drinks, Beverages	SMI-Texas	Steel
DPT Laboratories, Ltd.	Pharmaceuticals	San Antonio Aerospace	Aircraft Modification/Maint.
Friedrich Air Conditioning Co.	HVAC Systems	San Antonio Express-News	Daily Newspaper
Frito-Lay, Inc.	Snack Foods	Sino-Swearingen Aircraft Co.	Aircraft Design, Marketing/Sales
Kinetic Concepts, Inc.	Specialty Medical Products	Tesoro Corporation	Refining/Sales of Petroleum Prod.
L & H Packing Company	Meat Packing	The Scooter Store, Inc.	Medical & Dental Equipment
Lancer Corporation	Beverage Dispensing Equipment	Valero Energy Corporation	Refining/Sales of Petroleum Prod.
Martin Marietta Materials SW, Inc.	Concrete, Limestone, & Asphalt	Vulcan Materials	Materials, Cement, & Concrete
Medical:			
Advanced Living Technologies	Skilled Nursing Care Facilities	Methodist Healthcare System	General Acute Care Hospitals
Allied Primary Home Care Svcs.	Home Health Care Services	Methodist Specialty & Transplant Hosp.	Specialty Care Hospital
Baptist Health System	General Acute Care Hospitals	Metropolitan Methodist Hospital	General Acute Care Hospital
Brooke Army Medical Center	Military Hospital	Nix Health Care System	Hospital/Health Care Services
Caremark Prescription Service	Mail Order Pharmacy	Outreach Health Services	Home Health Care
Center for Health Care Services	Mental Health/Mental Retardation	San Antonio State Hospital	Mental Health/Mental Retardation
Christus Santa Rosa Health Care	General Acute Care Hospitals	San Antonio State School	Residential Care Facility
Girling Health Care, Inc.	Home Health Care Services	South Texas Blood & Tissue Center	Collect/Distribute Blood & Tissue
Guadalupe Valley Hospital	Hospital/Health Care Services	South Texas Veterans Health Care Sys.	Hospital/Health Care Services
Home Nursing & Therapy Svcs.	Home Health Care	Southwest General Hospital	Hospital/Health Care Services
Interim Healthcare San Antonio	Nurses' Registry	University of Texas Health Science Center at San Antonio	Medical School
McKenna Memorial Hospital	Hospital/Health Care Services	University Health System	Public Hospital/Clinics
Medical Team, Inc.	Home Health Care		
Methodist Children's Hospital	Children's Hospital		
Retail:			
Aaron Rents and Sells Furniture	Office & Residential Furniture	H-E-B Grocery Company	Groceries & Distribution
Ancira Enterprises	Automotive Sales & Service	HOLT CAT	Caterpillar Heavy Equipment
Brylane	Mail Order & Catalog Shopping	QVC San Antonio Inc.	Electronic Retail Sales
CVS/Pharmacy	Pharmacy Stores	R & L Foods, Inc.	Fast Foods
Dillard's Department Stores	Department Stores	Sun Harvest Farms, Inc.	Natural Food Grocery Stores
Eye Care Centers of America, Inc.	Eyewear	Target Stores	Discount Retail Stores
Foley's Department Stores	Department Stores	Twigland Fashions Ltd.	Women's Apparel
Gunn Automotive Group	Auto Dealerships		

¹ January 2006, *The Greater San Antonio Chamber of Commerce Largest Employer's Directory*.

(Table continues on next page.)

**Employers with 500 or More Employees in the San Antonio Metropolitan Area
(Includes Bexar, Comal, Guadalupe, and Wilson Counties)¹**

Firm	Product/Service	Firm	Product/Service
Services:			
AT & T Center	Sports/Events Arena	New Braunfels I.S.D.	Public School District
Able Body Labor	Temporary Staffing	Northside I.S.D.	Public School District
Administaff, Inc.	Professional Staffing	Our Lady of The Lake University	Higher Education, Private
Advance'd Temporaries, Inc.	Temporary Staffing	Palo Alto College	Junior/Community College
Advantage Rent-A-Car	Vehicle Rental	Parent/Child Inc.	Early Childhood Development
Air Force Village Foundation	Military Retirement Communities	Pioneer Drilling Company	Oil & Gas Drilling
Alamo Community College District	Public College District	RK Group	Catering
Alamo Heights I.S.D.	Public School District	Regal Cinemas	Movie Theaters
Alamodome	Domed Stadium	San Antonio College	Junior/Community College
Allen Tharp & Associates	Catering	San Antonio I.S.D.	Public School District
American Building Maintenance	Janitorial Contractor	Sanitors, Inc.	Commercial Janitorial
Archdiocese of San Antonio	Catholic Archdiocese	Schertz-Cibolo-Universal City I.S.D.	Public School District
Avance Inc.	Family Support & Education	Schlitterbahn Waterpark & Resort	Resort & Waterpark
Bill Miller Bar-B-Q Ent., Ltd	Restaurants & Catering	SeaWorld San Antonio	Entertainment/Amusement Park
Boeing Aerospace Support Center	Aerospace Support Center	Sears Customer Service Center	Customer Service Center
Cadbeck Staffing	Temporary Staffing	Securitas Security Services USA	Guard/Security Service
Calling Solutions, Inc.	Telemarketing	Seguin I.S.D.	Public School District
Citicorp – U.S. Service Center	Service Center	Six Flags Fiesta Texas	Entertainment/Amusement Park
Comal I.S.D.	Public School District	Somerset I.S.D.	Public School District
East Central I.S.D.	Public School District	South San Antonio I.S.D.	Public School District
Edgewood I.S.D.	Public School District	Southside I.S.D.	Public School District
Employers Resource Management	Temporary Staffing	Southwest I.S.D.	Public School District
Enterprise/Rent-A-Car Company	Vehicle Rental	Southwest Research Institute	Research & Development
Floresville I.S.D.	Public School District	Spectrum Health Club	Health Clubs
Frontier Enterprises	Restaurant Headquarters	St. Mary's University	Higher Education, Private
Goodwill Industries of S.A.	Vocational Training	St. Philip's College	Junior/Community College
Harcourt Assessment, Inc.	Test Publishers	Standard Aero, Inc.	Repair Aircraft Engines
Harlandale I.S.D.	Public School District	Taco Cabana, Inc.	Fast Food Restaurants
Hospital Klean of Texas, Inc.	Hospital Housekeeping	Talent Tree, Inc.	Temporary Staffing
Hyatt Hill Country Resort and Spa	Hotel Resort & Spa	Tansec Inc./Div. of Radio Shack	Alarms & Monitoring
Infonxx	Information Retrieval Services	Treco Services, Inc.	Janitorial, Window Cleaning
Judson I.S.D.	Public Education	Trinity University	Higher Education, Private
Little Caesar's of San Antonio, Inc.	Pizza Take Out Stores	University of Texas at San Antonio	Higher Education, Public
Lockheed Martin Kelly Aviation	Aviation Consultants	University of The Incarnate Word	Higher Education, Private
Luby's Cafeterias, Inc.	Cafeterias	VIP Temporaries	Temporary Staffing
MTC, Inc.	Full Service Restaurants	Waste Management Inc.	Refuse Systems
Marriott Rivercenter/Riverwalk Hotels	Hotels	Wendy's of San Antonio Inc.	Fast Food Restaurants
McDonald's-Haljohn, Inc.	Fast Food Restaurants	Westaff	Temporary Staffing
Mi Tierra Cafe & Bakery, Inc.	Restaurant & Bakery	Whataburger of Alice	Fast Food Restaurants
Morningside Ministries	Retirement & Nursing Homes	YMCA of Greater of San Antonio	Health & Wellness
Transportation, Communications, & Utilities:			
AT&T, Inc.	Voice, Data, Telecommunications	Time Warner	Voice, Data, Telecommunications
CPS Energy	Natural Gas & Electric Service	U.S. Postal Service	Postal Delivery
San Antonio Water System	Water Services	United Parcel Service	Parcel Delivery
Southwest Airlines	Air Transportation		
Wholesale:			
Advantage Sales & Marketing	Sales & Marketing	SYGMA Network, Inc.	Distributor - Groceries
CARQUEST Auto Parts	Automotive Replacement Parts	San Antonio Auto Auction	Auto Auction
Color Spot Nurseries/SW Division	Plant Nurseries	Tyson Foods, Inc.	Poultry Slaughtering & Packing

¹ January 2006, *The Greater San Antonio Chamber of Commerce Largest Employer's Directory*.

San Antonio Electric and Gas Systems

History and Management

The City acquired its electric and gas utilities in 1942 from the American Light and Traction Company, which had been ordered by the federal government to sell properties under provisions of the Holding Company Act of 1935. The bond ordinances authorizing the issuance of the currently outstanding Senior Lien Obligations, Junior Lien Obligations and Commercial Paper Notes establish management requirements and provide that the complete management and control of the City's electric and gas systems (the "EG Systems") is vested in a Board of Trustees consisting of five citizens of the United States of America permanently residing in Bexar County, Texas, known as the "City Public Service Board of Trustees, San Antonio, Texas" (referred to herein as the "CPS Board" or "CPS"). The Mayor of the City is a voting member of the Board, represents the City Council, and is charged with the duty and responsibility of keeping the City Council fully advised and informed at all times of any actions, deliberations, and decisions of the CPS Board and its conduct of the management of the EG Systems.

Vacancies in membership on the CPS Board are filled by majority vote of the remaining members. New CPS Board appointees must be approved by a majority vote of the City Council. A vacancy, in certain cases, may be filled by the City Council. The members of the CPS Board are eligible for re-appointment at the expiration of their first five-year term of office to one additional term. In 1997, the City Council ordained that CPS Board membership should be representative of the geographic quadrants established by the City Council. New CPS Board members considered for approval by the City Council will be those whose residence is in a quadrant that provides such geographic representation.

The CPS Board is vested with all of the powers of the City with respect to the management and operation of the EG Systems and the expenditure and application of the revenues therefrom, including all powers necessary or appropriate for the performance of all covenants, undertakings, and agreements of the City contained in the bond ordinances, except regarding rates, condemnation proceedings, and issuances of bonds, notes, or commercial paper. The CPS Board has full power and authority to make rules and regulations governing the furnishing of electric and gas service and full authority with reference to making extensions, improvements, and additions to the EG Systems, and to adopt rules for the orderly handling of CPS' affairs. It is empowered to appoint and employ all officers and employees and must obtain and keep in force a "blanket" type employees' fidelity and indemnity bond covering losses in the amount of not less than \$100,000.

The management provisions of the bond ordinances also grant the City Council authority to review CPS Board action with respect to policies adopted relating to research, development, and planning.

In 1997, CPS established a 15 member Citizens Advisory Committee ("CAC") to enhance its relationship with the community and to address the City Council's goals regarding broader community involvement with CPS. The CAC meets monthly and the primary goal of the CAC is to provide recommendations from the community on the operations of CPS for use by the CPS Board and CPS staff. Representing the various sectors of CPS' service area, the CAC encompasses a broad range of customer groups in order to identify their concerns and understand their issues.

Service Area

The CPS electric system serves a territory consisting of substantially all of Bexar County and small portions of the adjacent counties of Comal, Guadalupe, Atascosa, Medina, Bandera, Wilson, and Kendall. Certification of this CPS electric service area has been approved by the Public Utility Commission of Texas (the "PUCT").

CPS is currently the exclusive provider of electric service within the service area, including the provision of electric service to some Federal military installations located within the service area that own their own distribution facilities. As discussed below under "Electric Utility Restructuring in Texas; Senate Bill 7", until and unless the City Council and the CPS Board exercise the option to opt-in to retail electric competition (called "Texas Electric Choice" by the PUCT), CPS has the sole right to serve as the retail electric energy provider in its service area. On April 26, 2001, after a thorough feasibility study was conducted and reviewed, the City Council passed a resolution

stating that the City did not intend to opt-in to the deregulated electric market beginning January 1, 2002, the date Texas Electric Choice became effective. Senate Bill 7 (“SB 7”), adopted by the Texas Legislature in 1999, provides that electric “opt-in” decisions are to be made by the governing body or the body vested with the power to manage and operate a municipal utility such as CPS. Given the relationship of the CPS Board and the City Council, any decision to opt-in to competition would be based upon the adoption of resolutions of both the CPS Board and the City Council. If the City and CPS choose to opt-in, other retail electric energy suppliers would be authorized to offer retail electric energy in the CPS service area and CPS would be authorized to offer retail electric energy in any other areas open to retail competition in the Electric Reliability Council of Texas (“ERCOT”). ERCOT is the independent entity that monitors and administers the flow of electricity within the interconnected grid that operates wholly within Texas. (See “Electric Utility Restructuring In Texas; Senate Bill 7.”). CPS has the option of acting in the role of the “Provider of Last Resort” for its service area in the event it and the City choose to opt-in.

In addition to the area served at retail rates, CPS sells electricity at wholesale prices to the Floresville Electric Light & Power System, the City of Hondo, and the City of Castroville. These wholesale supply agreements have remaining terms ranging from one to twelve years until expiration, although some of the agreements provide for automatic extension or conditional early termination. CPS will seek additional opportunities to enter into long-term wholesale electric power agreements in the future. The requirements under the existing and any new wholesale agreements would be firm energy obligations of CPS.

The CPS gas system serves the City and its environs, although there is no certificated CPS gas service area. In Texas, no legislative provision or regulatory procedure exists for certification of natural gas service areas. CPS competes against other gas supplying entities on the periphery of its service area. Pursuant to the authority provided by Section 181.026, Texas Utilities Code, among other applicable laws, the City has executed a license agreement (“License Agreement”) with the City of Grey Forest, Texas (“Licensee”), dated as July 28, 2003, for a term through May 31, 2028. Pursuant to this License Agreement, the City permits the Licensee to provide, construct, operate and maintain certain natural gas lines within the boundaries of the City which it originally established in 1967 and to provide extensions and other improvements thereto upon compliance with the provisions of the License Agreement and upon the payment to the City of a quarterly license fee of 3.0% of the gross revenues received by the Licensee from the sale of natural gas within the Licensed Area (as defined in the License Agreement). Thus, in the Licensed Area, CPS is in direct competition with Grey Forest Utilities as a supplier of natural gas.

CPS has franchise agreements with 28 incorporated communities (“Suburban Cities”) in the San Antonio area. These franchise agreements permit CPS to operate its facilities in the cities' streets and public ways in exchange for a franchise fee of 3% on electric and natural gas revenues earned within their respective municipal boundaries. The majority of these agreements expire in 2010; the others expire in December 2006, 2011, 2017, 2028, and 2029.

Retail Service Rates

Under the Texas Public Utility Regulatory Act (“PURA”), significant original jurisdiction over the rates, services, and operations of “electric utilities” is vested in the PUCT. In this context, “electric utility” means an electric investor-owned utility. Since the electric deregulation aspects of SB 7 became effective on January 1, 2002, the PUCT’s jurisdiction over the electric investor-owned utility (“IOU”) companies primarily encompasses only the transmission and distribution functions. PURA generally excludes municipally-owned utilities (“Municipal Utilities”), such as CPS, from PUCT jurisdiction, although the PUCT has jurisdiction over electric wholesale transmission rates. Under the PURA, a municipal governing body or the body vested with the power to manage and operate a Municipal Utility such as CPS has exclusive jurisdiction to set rates applicable to all services provided by the Municipal Utility with the exception of electric wholesale transmission activities and rates. Unless and until the City Council and CPS Board choose to opt-in to electric retail competition, CPS retail service electric rates are subject to appellate, but not original rate regulatory jurisdiction by the PUCT in areas that CPS serves outside the City limits. To date, no such appeal to PUCT of CPS retail electric rates has ever been filed. CPS is not subject to the annual PUCT gross receipts fee payable by electric utilities. (See “Electric Utility Restructuring in Texas; Senate Bill 7” herein.)

The Texas Railroad Commission (“TRC”) has significant original jurisdiction over the rates, services, and operations of all natural gas utilities in the State. Municipal Utilities such as CPS are generally excluded from

regulation by the TRC, except in matters related to natural gas safety. CPS retail gas service rates applicable to rate payers outside San Antonio are subject to appellate, but not original rate regulatory jurisdiction, by the TRC in areas that CPS serves outside the City limits. To date, no such appeal to the TRC of CPS retail gas rates has ever been filed. In the absence of a contract for service, the TRC also has jurisdiction to establish gas transportation rates for service to State agencies by a Municipal Utility. A Municipal Utility is also required to sell gas to and transport State-owned gas for “public retail customers,” including State agencies, State institutes of higher education, public school districts, U.S. military installations, and U.S. Veterans Affairs facilities, at rates provided by written contract between the Municipal Utility and the buyer entity. If agreement to such a contract cannot be reached, a rate would be set by the legal and relevant regulatory body.

The City has covenanted and is obligated under the bond ordinances, as provided under the rate covenant, to establish and maintain rates and collect charges in an amount sufficient to pay all maintenance and operating expenses of the EG Systems and to pay the debt service requirements on all revenue debt of the EG Systems, including all other payments prescribed in the bond ordinances.

Rate changes over the past 16 years have consisted of a 4.0% combined electric and gas base rate increase effective January 31, 1991; a Large Volume Gas rate effective July 31, 1992, which was offered to Large Gas Customers whose monthly gas usage exceeded 550 MCF per month and enabled them to reduce bills by approximately 8.8%; a Super Large Power (“SLP”) electric rate effective January 4, 1994, which reduced the basic rates to customers having loads greater than 5,000 KW per month and annual load factors greater than 41% by approximately 10.1%; and a 3.5% electric base rate adjustment approved by City Council on September 30, 2004. The latter adjustment became effective on May 19, 2005, and a 12.15 gas base rate adjustment effective June 26, 2006. The 2005 electric rate adjustment was intended to offset the incremental costs to be incurred due to acquiring an additional 12% share in the South Texas Project. This acquisition was completed in May 2005. CPS projects that the net effect of the base rate adjustment and fuel cost savings from additional nuclear-fueled generation will result in lower overall bills for CPS’ electric customers (See “Electric System – Generating System” herein). CPS also offers a monthly contract for renewable energy service (currently this is wind generated electricity) under Rider E15, which became effective May 2000. The rate for Rider E15 was reduced to its current level effective on September 30, 2002. A rider to the SLP rate, the Economic Incentive Rider E16, became effective March 10, 2003, and offers discounts off the SLP demand charge for a period up to four years for new or added load of at least 10 megawatts (“MW”). Under certain conditions, the discount may be extended an additional three years. Customers that choose Economic Incentive Rider E16 must also meet City employment targets and targets for purchases of goods or services from local businesses in order to qualify. CPS also has rates that permit recovery of certain miscellaneous customer charges and for extending lines to provide gas and electric service to its customers. In May 2005, the CPS Board adopted a change to its policies for both miscellaneous customer charges and line extensions, to become effective January 1, 2006, to increase charges that had not been raised since 1986. On December 15, 2005, the City Council adopted Ordinance Nos. 101819 and 101820 approving certain of the price changes in the CPS Board-approved policy; however, the City ordinance prevents recovery of increased line extension charges from developers of affordable housing and the City delayed implementation of certain miscellaneous charges until April 1, 2006 (fees for disconnection, reconnection, and field notification).

Each of CPS’ retail and wholesale rates contains an electric fuel adjustment or gas cost adjustment clause, which provides for current recovery of fuel costs. The fuel cost recovery adjustments are set at the beginning of each CPS billing cycle month.

Transmission Access and Rate Regulation

Pursuant to amendments made by the Texas Legislature in 1995 to the PURA (“PURA95”), Municipal Utilities, including CPS, became subject to the regulatory jurisdiction of the PUCT for transmission of wholesale energy. PURA95 requires the PUCT to establish open access transmission on the interconnected Texas grid for all utilities, co-generators, power marketers, independent power producers, and other transmission customers.

The 1999 Texas Legislature amended the PURA95 to expressly authorize rate authority over Municipal Utilities for wholesale transmission and to require that the postage stamp method be used exclusively for pricing wholesale transmission transactions. The PUCT in late 1999 amended its transmission rule to incorporate fully the postage stamp pricing method. In general, the postage stamp method results in transmission payments to other

transmission owners by a compact urban utility like CPS that exceed its receipts from other utilities for use of its own transmission facilities. CPS' wholesale open access transmission charges are set out in tariffs filed at the PUCT, and are based on its transmission cost of service approved by the PUCT, representing CPS' input to the calculation of the statewide postage stamp pricing method. The PUCT's rule, consistent with provisions in PURA §35.005(b), also provides that the PUCT may require construction or enlargement of transmission facilities in order to facilitate wholesale transmission service. Pursuant to P.U.C. Docket No. 31540, "Proceeding to Consider Protocols to Implement a Nodal Market in the Electric Reliability Council of Texas Pursuant SUBST. R. 25.501," the PUCT has made substantial progress in evaluating the shift from postage stamp pricing to nodal pricing for transmission transactions. Until the PUCT takes final action on nodal pricing, it will not be possible to predict the effects on CPS' transmission costs or its ability to recover costs from other participants in ERCOT.

Electric Utility Restructuring in Texas; Senate Bill 7. During the 1999 legislative session, the Texas Legislature enacted SB 7, providing for retail electric open competition. This began on January 1, 2002. SB 7 continues electric transmission wholesale open access, which came into effect in 1997 and requires all transmission system owners to make their transmission systems available for use by others at prices and on terms comparable to each respective owner's use of its system for its own wholesale transactions. SB 7 also fundamentally redefines and restructures the Texas electric industry. The following discussion of SB 7 applies primarily to ERCOT.

SB 7 includes provisions that apply directly to Municipal Utilities such as the CPS, as well as other provisions that govern IOUs and electric co-operatives ("Electric Co-ops"). As of January 1, 2002, SB 7 allows retail customers of IOUs to choose their electric energy suppliers. SB 7 also allows retail customers of those Municipal Utilities and Electric Co-ops that elect, on or after that date, to participate in retail electric competition. Provisions of SB 7 that apply to the CPS electric system, as well as provisions that apply only to IOUs and Electric Co-ops are described below, the latter for the purpose of providing information concerning the overall restructured electric utility market in which CPS and the City could choose to directly participate in the future.

SB 7 required IOUs to separate their retail energy service activities from regulated utility activities by September 1, 2000, and to unbundle their generation, transmission/distribution, and retail electric sales functions into separate units by January 1, 2002. An IOU may choose to sell one or more of its lines of business to independent entities, or it may create separate but affiliated companies, and possibly operating divisions. If so, these new entities may be owned by a common holding company, but each must operate largely independent of the others. The services offered by such separate entities must be available to other parties on a non-discriminatory basis. Municipal Utilities and Electric Co-ops which open their service territories ("opt-in") to retail electric competition are not required to, but may, unbundle their electric system components.

SB 7 also provides a number of consumer protection provisions. Each service area within Texas that participates in retail competition has a designated "Provider of Last Resort"; those Providers of Last Resort serving in former service areas of IOUs are selected and approved by the PUCT. The Provider of Last Resort is an REP that must offer to sell electricity to any retail customer in its designated area at a standard rate approved by the PUCT. The Provider of Last Resort must also serve any customer whose REP has failed to provide service. Each Municipal Utility and Electric Co-op that opts-in to retail competition may designate itself or another qualified entity as the Provider of Last Resort for its service territory. In such cases, the respective Municipal Utility or Electric Co-op, not the PUCT will set the electric rates for such respective Provider of Last Resort.

Beginning September 1, 1999, each IOU was required to freeze its then existing rates (except for a fuel factor pass through) and was required to continue to serve its retail customers at such rates until 2002. Beginning January 1, 2002, the unbundled REP of the IOU that held the certificate to provide retail service to an area ("Affiliated REP") was required to reduce electric rates by 6% below the frozen rates and offer that reduced rate ("price to beat") to all residential and small commercial retail customers in the area formerly served by the IOU. The Affiliated REP was not allowed to sell electricity to residential or small commercial customers at any other rate until the earlier of either 40% of the residential or small commercial customers in the area had chosen to be served by other REPs or until January 1, 2005. SB 7 does allow Affiliated REPs to compete for industrial customers and for certain aggregated commercial loads owned by a common entity. The price to beat provisions of SB 7 currently has no direct impact on CPS.

Under SB 7, IOUs may recover a portion of their “stranded costs” (the net book value of certain “non-economic” assets less market value and certain “above market” purchased-power costs) and “regulatory assets”, which is intended to permit recovery of the difference between the amount necessary to pay for the assets required under prior electric regulation and the amount that can be collected through market-based rates in the open competition market. SB 7 establishes the procedure to determine the amount of IOU stranded costs and regulatory assets. The PUCT has determined the stranded costs, which have been and will be collected through a non-bypassable competitive transition charge collected from the end retail electric users within the IOU's service territory as it existed on May 1, 1999. The charge is collected primarily as an additional component to the rate for the use of the retail electric distribution system delivering electricity to such end user.

IOUs may recover a certain portion of their respective stranded costs through the issuance of bonds, with a maturity not to exceed 15 years, whereby the principal, interest and reasonable costs of issuing, servicing and refinancing such bonds is secured by a qualified rate order of the PUCT that creates the “competitive transition charge”. Neither the State of Texas nor the PUCT may amend the qualified rate order in any manner that would impair the rights of the “securitized” bondholders.

Additional Impacts of Senate Bill 7. Municipal Utilities and Electric Co-ops are largely exempt from the requirements of SB 7 that apply to IOUs. While IOUs became subject to retail competition beginning on January 1, 2002, the governing bodies of Municipal Utilities and Electric Co-ops have the sole discretion to determine whether and when to opt-in to retail competition. However, if a Municipal Utility or Electric Co-op has not voted to opt-in, it will not be able to compete for retail energy customers at unregulated rates outside its traditional electric service area or territory.

SB 7 preserves the PUCT's regulatory authority over electric transmission facilities and open access to such transmission facilities. SB 7 provides for an independent transmission system operator (an ISO as previously defined) that is governed by a board comprised of market participants and independent members and is responsible for directing and controlling the operation of the transmission network within ERCOT. The PUCT has designated ERCOT as the ISO for the portion of Texas within the ERCOT area. In addition, SB 7 (as amended by the Texas Legislature after 1999) directs the PUCT to determine electric wholesale transmission open access rates on a 100% “postage stamp” pricing methodology.

The greatest potential impact on CPS' electric system from SB 7 could result from a decision by the City Council and the Board to participate in a fully competitive market, particularly in light of the fact that CPS is among the lowest cost producers of electric energy in Texas. On April 26, 2001, the City Council passed a resolution stating that the City did not intend to opt-in to the deregulated electric market beginning January 1, 2002. However, CPS currently believes that it is taking all steps necessary to prepare for possible competition in the unregulated energy market, should the City Council and the Board make a decision to opt-in.

Any future decision of the City Council and the Board to participate in full retail competition would permit CPS to offer electric energy service to customers located in areas participating in retail choice that are not presently within the certificated service area of CPS. The City Council and the Board could likewise choose to open the CPS service area to competition from other suppliers while choosing not to have CPS compete for retail customers outside its certified service area.

As discussed above, Municipal Utilities and Electric Co-ops will also determine the rates for use of their distribution systems after they open their territories to competition, although the PUCT has established by rule the terms and conditions applicable to have access to those systems. SB 7 also permits Municipal Utilities and Electric Co-ops to recover their stranded costs through collection of a non-bypassable transition charge from their customers if so determined by such entities through procedures that have the effect of procedures available to IOUs under SB 7. Unlike IOUs, the governing body of a Municipal Utility determines the amount of stranded costs to be recovered pursuant to rules and procedures established by such governing body. Municipal Utilities and Electric Co-ops are also permitted to recover their respective stranded costs through the issuance of bonds in a similar fashion to the IOUs. Any decision by CPS as to the magnitude of its stranded costs, if any, would be made in conjunction with the decision as to whether or not to participate in retail competition.

A Municipal Utility that decides to participate in retail competition and to compete for retail customers

outside its traditional service area will be subject to a PUCT-approved code of conduct governing affiliate relationships and anti-competitive practices. The PUCT has established by a standard rule the terms and conditions, but has no jurisdiction over the rates, for open access by other suppliers to the distribution facilities of Municipal Utilities electing to compete at retail. If a Municipal Utility decides to participate in retail competition, its customers are subject to being charged a PUCT-approved System Benefit Fund fee per megawatt hour beginning six months prior to implementation of customer choice. The fee is a contribution to a statewide fund targeted at property tax replacement, low-income programs and customer education.

Among other provisions, SB 7 provides that nothing in the act or in any rule adopted under it may impair any contracts, covenants, or obligations between municipalities and bondholders of revenue bonds issued by municipalities and that nothing in the act may impair the tax-exempt status of municipalities or compel them to use facilities in a manner that violates any bond covenants or other exemption of interest or tax-exempt status. The bill also improves the competitive position of Municipal Utilities by allowing local governing bodies, whether or not they implement retail choice, to adopt alternative procurement processes under which less restrictive competitive bidding requirements can apply and to implement more liberal policies for the sale and exchange of real estate. Also, matters affecting the competitiveness of Municipal Utilities are made exempt from disclosure under the open meetings and open records acts and the right of municipal utilities to enter into risk management and hedging contracts for fuel and energy is clarified. See “FUEL SUPPLY”, “WHOLESALE POWER MARKETING”, and “RISK MANAGEMENT” for discussion of CPS’ Price Risk Management Program.

During its 79th Legislative Session in 2005, the Texas Legislature reviewed the mission and performance of the PUCT, as required by the Texas Sunset Act. This Act provides that the Sunset Commission, composed of legislators and public members, periodically evaluate a state agency to determine if the agency is still needed, and what improvements are needed to ensure that tax dollars are appropriately utilized. Based on recommendations of the Sunset Commission, the Texas Legislature ultimately decides whether an agency continues to operate into the future.

The 79th Legislature in its review of the PUCT, reauthorized the agency until 2011. Reforms were enacted to increase the accountability of ERCOT, including added regulatory scrutiny and governance changes that add independence while preserving input from industry experts. An “independent market monitor” selected by and reporting to the PUCT, was institutionalized to help guard against manipulation in the Texas wholesale electric market. No significant, direct impact on CPS is anticipated as a result of this legislation.

Post Senate Bill 7 Wholesale Market Design Developments. In the summer of 2003, the PUCT adopted rules requiring that ERCOT transition from a zonal to a nodal wholesale market by October 1, 2006, and requiring that new protocols to accomplish this transition be submitted to the PUCT for review. Implementation of the nodal market will include, among other elements: direct assignment of the costs of local transmission congestion to market participants that cause the congestion; implementation of an integrated, financially binding day-ahead market; and nodal energy prices for resources and zonal energy prices for loads. Consistent with the rule, ERCOT and industry stakeholders have developed and submitted to the PUCT protocols and proposed energy load zones to implement these market design elements, together with an independent cost-benefit analysis. The PUCT in 2005 reaffirmed its intent to implement the nodal market in ERCOT, but modified the implementation date to January 1, 2009. In December 2005, the PUCT conducted a hearing on the nodal protocols submitted by ERCOT, and in April 2006 it issued an order approving the implementation of the nodal market. ERCOT has begun its process of design specification and implementation, which will be followed by design specification and implementation by market participants, including CPS. These activities will continue through early 2008, followed by integration testing and trials leading to the January 1, 2009 implementation date.

Environmental Restrictions of Senate Bill 7. SB 7 contains specified emissions reduction requirements for certain older electric generating units, which would otherwise be exempt from the Texas Commission on Environmental Quality (“TCEQ”) permitting program by virtue of “grandfathered” status. Under SB 7, annual emissions of nitrogen oxides (“NOx”) from such units were reduced by 50% from 1997 levels, beginning May 1, 2003. These emissions have been reported on a yearly basis and CPS has met the requirements of its NOx cap for the applicable units for the past three compliance years. CPS has final State permits from the TCEQ, for its five CPS generating stations, comprising 12 gas-fired units. CPS may require future additional expenditures for emission control technology.

Although SB 7 instituted many of the changes to environmental emission controls which affect grandfathered electric generating plants, another TCEQ regulation, Chapter 117, is directed at all units, including CPS' coal plants. These regulations required a 50% reduction in NOx emissions beginning May 1, 2005 system-wide on an annual basis. CPS' power plants are subject to the Chapter 117 cap for the compliance period of May 1, 2005 to April 2006. In addition, as a result of J.K. Spruce Plant Unit 2 ("JKS 2") air permitting process, CPS has committed to tighter NOx emission limitations than what is required under Chapter 117 at the Calaveras Lake site once the JKS 2 unit comes on line. The final Clean Air Interstate Rule has imposed even more NOx restrictions on CPS power plants. Changes to environmental emission controls may have the greatest effect on coal plants. For example, mercury emission limits have been finalized by the Environmental Protection Agency ("EPA"), which may require new controls at the coal plants in the near future. Further statutory changes and additional regulations may change existing cost assumptions for electric utilities. While it is too early to determine the extent of any such changes, such changes could have a material impact on the cost of power generated at affected electric generating units.

Response to Competition

Strategic Planning Initiatives. CPS has a comprehensive corporate strategic plan that is designed to make CPS more efficient and competitive, while delivering value to customers and the City. On August 22, 2005, the CPS Board approved a new strategic plan, developed by a cross functional team. The plan builds on the CPS mission, vision, and core values as well as long-term goals adopted in 2004, as part of the Vision 2020 process. The plan focuses efforts on five areas – growth, organization development, business information, process improvement, and transition to competition. Each strategy has an executive leading the implementation.

Mission statements, strategic objectives, strategies and metrics and targets are an integral part of each business plan. Major initiatives and key action plans necessary to accomplish the objectives and meet or exceed the targets are also included in each plan. Status reports are provided to the Board and senior management on a regular basis. A new position, Strategic Planning Manager, has been created to lead the ongoing implementation and oversight of the strategic plan.

Debt and Asset Management Program. CPS has developed a debt and asset management program (the "Debt Management Program") for the purposes of lowering the debt component of energy costs, maximizing the effective use of cash and cash equivalent assets, and enhancing financial flexibility. An important part of the Debt Management Program is debt restructuring through the prudent employment of variable rate debt and possible interest rate swap contracts. It is anticipated, however, that the variable rate exposure of CPS will not exceed 25% of total outstanding debt. The program also focuses on the use of unencumbered cash and available cash flow to redeem debt ahead of scheduled maturities as a means of reducing outstanding debt. The Debt Management Program is designed to lower interest costs, fund strategic initiatives, and increase net cash flow.

Electric System

Generating System. CPS operates 19 electric generating units, three of which are coal-fired and 16 of which are gas-fired. Some of the gas-fired generating units may also burn fuel oil, which provides greater fuel flexibility and reliability. With the acquisition of an additional 300 MW purchased from AEP Texas Central Company ("AEP TCC"), as of May 19, 2005, CPS has a 40.0% interest in STP's two nuclear generating units. When both units of STP operate as planned, they supply approximately one-third of CPS' annual electric load. The nuclear units supplied 33.9% of the electric system load during fiscal year 2005-2006.

On September 30, 2004, CPS received approval for a change in the amount it charges for retail and certain wholesale rates, which went into effect on May 19, 2005. This \$41 million base rate adjustment was designed to support the issuance of the 2004 Junior Lien Obligations and CPS' increased share of operation and maintenance expenses at STP. (See "Retail Service Rates").

STP Participant Ownership - Participants in the STP and their shares therein are as follows (MW capacity are approximations):

Participants	Ownership	
	%	MW
NRG Energy	44.0	1,127.5
City Public Service	40.0	1,025.0
City of Austin - Austin Energy	<u>16.0</u>	<u>410.0</u>
	<u>100.0</u>	<u>2,562.5</u>

STP is maintained and operated by a non-profit Texas corporation (“STP Nuclear Operating Company”) financed and controlled by the owners pursuant to an operating agreement among the owners and STP Nuclear Operating Company. Currently, a four-member board of directors governs the STP Nuclear Operating Company, with each owner appointing one member to serve with the STP Nuclear Operating Company's chief executive officer. All costs and output continue to be shared in proportion to ownership interests.

STP Units 1 and 2 each have a 40-year NRC license that expires in 2027 and 2028, respectively. No firm decision has been made with respect to license extension; however, under NRC regulations, the STP owners may not make a license extension request until the plant licenses are within 20 years of the license expiration date.

During the twelve-months ended January 31, 2006, the STP Units 1 and 2 operated at approximately 90.1% and 90.6% of net capacities, respectively. Unit 1 completed a normal refueling outage in spring 2005. Unit 2 completed a normal refueling outage in fall of 2005.

Qualified Scheduling Entity. CPS and Texas Genco operated under the Joint Operating Agreement from July 1, 1996 until the termination of that agreement on January 25, 2006. The agreement provided that the two entities jointly dispatch their generating plants (other than STP) in order to take advantage of the most efficient plants and favorable fuel prices to serve the combined loads of both entities. Texas Genco acted as the Qualified Scheduling Entity (“QSE”) for scheduling both its and CPS' generation schedules with ERCOT. CPS and Texas Genco shared equally the benefits achieved through joint dispatch of their combined portfolio of power plants.

Due to changes in market conditions and the ERCOT market structure, Texas Genco terminated the agreement. CPS and Texas Genco completed an amicable and planned separation. CPS is now operating as an independent Level 4 QSE representing all of CPS' assets and load.

Transmission System. CPS maintains a transmission network for the movement of large amounts of electric power from the generating stations to various parts of the service area and to or from neighboring utilities as required. This network is composed of 138 and 345 kV lines with autotransformers to provide the necessary flexibility in the movement of bulk power.

Distribution System. The distribution system is supplied by 72 substations strategically located on the high voltage 138 kV transmission system. The central business district of the City is served by nine underground networks, each consisting of four primary feeders operated at 13.8 kV, transformers equipped with network protectors, and both a 4-wire 120/208 volt secondary grid system and a 4-wire 277/480 volt secondary spot system. This system is well designed for both service and reliability.

Approximately 7,580 circuit miles (three-phase equivalent) of overhead distribution lines are included in the distribution system. These overhead lines also carry secondary circuits and street lighting circuits. The underground distribution system consists of approximately 321 miles of three-phase distribution lines, 83 miles of three-phase Downtown Network distribution lines, and 3,738 miles of single-phase underground residential distribution lines. Many of the residential subdivisions added in recent years are served by underground distribution systems. At January 31, 2006, the number of street lights in service was 71,134. The vast majority of the lights are high-pressure, sodium vapor units.

Gas System

Supply Pressure System. The supply pressure system consists of a network of approximately 200 miles of steel mains that range in size from 4 to 30 inches. The entire system is coated and cathodically protected to mitigate corrosion. The supply pressure system operates at pressures between 50 psig and 274 psig, and supplies gas to 269 pressure regulating stations throughout the gas distribution system which reduce the pressure to between 9 psig and 59 psig for the distribution system. A Supervisory Control and Data Acquisition computer system ("SCADA") monitors the gas pressure and flow rates at many strategic locations within the supply pressure system, and most of the critical pressure regulating stations and isolation valves are remotely controlled by SCADA.

Distribution System. The gas distribution system consists of approximately 4,400 miles of 2 to 16-inch steel mains and 1-1/4 to 6-inch high-density polyethylene (plastic) mains. The distribution system operates at pressures between 9 psig and 59 psig. All steel mains are coated and cathodically protected to mitigate corrosion. The vast majority of the gas services are connected to the distribution system, and the gas normally undergoes a final pressure reduction at the gas meter to achieve the required customer service pressure. Critical areas of the distribution system are remotely monitored by SCADA.

Implementation of New Accounting Policies

For the fiscal year ended January 31, 2005, CPS adopted the provisions of the GASB Statement No. 40, Deposit and Investment Risk Disclosures. On January 31, 2005, the investment policies of CPS and the STP Decommissioning Trust were amended to include specific language requirements associated with GASB Statement No. 40, Deposit and Investment Risk Disclosures. Simultaneously, the guidelines of the Employee Benefit Plans were formalized in writing to also include the language requirements of GASB Statement No. 40. The adoption of this guidance did not affect CPS' financial position or results of operations. However, it did result in additional reporting disclosures that have been incorporated into the financial statements.

Recent Financial Transactions

On December 1, 2005, CPS remarketed \$157,000,000 of its Series 2004 variable rate demand obligations for a two-year term with approval from the CPS Board and City Council. CPS will pay an interest rate of 3.55% through November 30, 2007 at which time these bonds will be remarketed again.

On January 1, 2006, CPS extended the 2003 Junior Lien Bonds, Standby Bond Purchase Agreement's ("SBPA") expiration date to January 31, 2008 for an annual savings of \$112,500.

On August 9, 2006, CPS priced \$384,185,000 in revenue bonds which will close on August 31, 2006. The bond proceeds will be used to finance costs associated with constructing capital improvements of the EG Systems.

On August 11, 2006, CPS cash defeased \$106,440,000 in New Series 1997 revenue and refunding bonds. This allowed CPS to reduce its debt service by defeasing some of its higher cost debt.

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City Public Service Historical Net Revenues and Coverage¹

(Dollars in Thousands)

	Fiscal Years Ended January 31,					
	2001	2002	2003	2004	2005	2006
Gross Revenues ²	\$ 1,389,239	\$ 1,249,869	\$ 1,271,656	\$ 1,526,904	\$1,473,254	\$1,754,927
Maintenance & Operating Expenses	754,146	688,876	740,161	942,471	882,508	1,057,035
Available For Debt Service	<u>\$ 635,093</u>	<u>\$ 560,993</u>	<u>\$ 531,495</u>	<u>\$ 584,433</u>	<u>\$ 590,746</u>	<u>\$ 697,892</u>
Actual Principal and Interest Requirements:						
Senior Lien Obligations ³	<u>\$ 208,567</u>	<u>\$ 212,274</u>	<u>\$ 211,831</u>	<u>\$ 230,250</u>	<u>\$ 245,984</u>	<u>\$ 256,442</u>
Junior Lien Obligations ⁴	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 2,111</u>	<u>\$ 4,386</u>	<u>\$ 10,964</u>
Actual Coverage-Senior Lien	3.05x	2.64x	2.51x	2.54x	2.40x	2.72x
Actual-Senior and Junior Lien	3.05x	2.64x	2.51x	2.52x	2.36x	2.61x

¹ Unaudited

² Calculated in accordance with the ordinances.

³ Net of accrued interest where applicable.

⁴ Series 2003 Junior Lien Obligations were issued May 15, 2003. Series 2004 Junior Lien Obligations were issued November 18, 2004. Actual interest payments.

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San Antonio Water System

History and Management

In 1992, the City Council consolidated all of the City's water related functions, agencies, and activities into one agency. This action was taken due to the myriad of issues confronting the City related to the development and protection of its water resources. The consolidation provided the City with a singular, unified voice of representation when promoting or defending the City's goals and objectives for water resource protection, planning, and development with local, regional, state, and federal water authorities and officials.

Final City Council approval for the consolidation was given on April 30, 1992 with the approval of Ordinance No. 75686 (the "System Ordinance"), which created the City's water system ("SAWS"), a single, unified system consisting of the former City departments comprising the waterworks, wastewater, and water reuse systems, together with all future improvements and additions thereto, and all replacements thereof. In addition, the System Ordinance authorizes the City to incorporate into SAWS a stormwater system and any other water related system to the extent permitted by law.

The City believes that establishing SAWS has helped to reduce the costs of operating, maintaining, and expanding the water systems and has allowed the City greater flexibility in meeting future financing requirements. More importantly, it has allowed the City to develop, implement, and plan for its water needs through one agency.

The complete management and control of SAWS is vested in a board of trustees (the "SAWS Board") currently consisting of seven members, including the City's Mayor and six persons who are residents of the City or reside within the SAWS service area. With the exception of the Mayor, all SAWS Board members are appointed by the City Council for four-year staggered terms and are eligible for reappointment for one additional four-year term. Four SAWS Board members must be appointed from four different quadrants in the City, and two SAWS Board members are appointed from the City's north and south sides, respectively. SAWS Board membership specifications are subject to future change by City Council.

With the exception of fixing rates and charges for services rendered by SAWS, condemnation proceedings, and the issuance of debt, the SAWS Board has absolute and complete authority to control, manage, and operate SAWS, including the expenditure and application of gross revenues, the authority to make rules and regulations governing furnishing to customers, and their subsequent payment for, SAWS' services, along with the discontinuance of such services upon the customer's failure to pay for the same. The SAWS Board, to the extent authorized by law and subject to certain various exceptions, also has authority to make extensions, improvements, and additions to SAWS and to acquire by purchase or otherwise properties of every kind in connection therewith.

Service Area

SAWS provides water and wastewater service to the majority of the population within the corporate limits of the City and Bexar County, which totals approximately 1.6 million residents. SAWS employs approximately 1,600 personnel and maintains over 9,100 miles of water and sewer mains.

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Historical Water Consumption (Million Gallons) ¹

<u>Fiscal Year Ended</u>	<u>Daily Average</u>	<u>Peak Day</u>	<u>Peak Month</u>	<u>Metered Usage</u>	<u>Metered Water Revenue</u>
05/31/2001	155	267	July	53,047	73,166,293
12/31/2001 ²	159	274	July	53,077	74,541,211
12/31/2002	143	222	August	51,850	77,801,600
12/31/2003	150	303	August	50,576	76,913,150
12/31/2004	144	295	August	49,366	77,113,717
12/31/2005	172	278	July	55,005	98,869,037

¹ Unaudited.

² On April 3, 2001, the SAWS Board approved the changing of the fiscal year from a year-end of May 31 to December 31. Report is for the twelve (12) months ending December 31, 2001.

Source: SAWS.

Water Consumption by Customer Class (Million Gallons) ¹

	<u>December 31, 2005</u>	<u>December 31, 2004</u>	<u>December 31, 2003</u>	<u>December 31, 2002</u>	<u>December 31, 2001 ²</u>	<u>May 31, 2001</u>
Residential	31,114	27,173	27,760	28,372	29,003	28,694
Commercial	12,991	11,746	11,730	11,942	12,371	12,384
Apartment	8,004	7,663	7,794	7,791	7,718	7,783
Industrial	2,122	2,089	2,473	2,696	2,670	2,737
Wholesale	121	99	136	173	531	535
Municipal	652	596	683	876	784	914
	<u>55,005</u>	<u>49,366</u>	<u>50,576</u>	<u>51,850</u>	<u>53,077</u>	<u>53,047</u>

¹ Unaudited.

² On April 3, 2001, the SAWS Board approved the changing of the fiscal year from a year-end of May 31 to December 31. Report is for the twelve (12) months ending December 31, 2001.

Source: SAWS.

SAWS System

SAWS includes all water resources, properties, facilities, and plants owned, operated, and maintained by the City relating to supply, storage, treatment, transmission, and distribution of treated potable water, chilled water, and steam (collectively, the “waterworks system”), collection and treatment of wastewater (the “wastewater system”), and treatment and recycle of wastewater (the “recycle water system”) (the waterworks system, the wastewater system, and the recycle water system, collectively, the “system”). The system does not include any “Special Projects,” which are declared by the City, upon the recommendation of the SAWS Board, not to be part of the system and are financed with obligations payable from sources other than ad valorem taxes, certain specified revenues, or any water or water-related properties and facilities owned by the City as part of its electric and gas system.

In addition to the water related utilities that the SAWS Board has under its control, on May 13, 1993, the City Council approved an ordinance establishing initial responsibilities over the stormwater quality program with the SAWS Board and adopted a schedule of rates to be charged for stormwater drainage services and programs. As of the date hereof, the stormwater program is not deemed to be a part of the system.

Waterworks System. The City originally acquired its waterworks system in 1925 through the acquisition of the San Antonio Water Supply Company, a privately owned company. Since such time and until the creation of SAWS in 1992, management and operation of the waterworks system was under the control of the City Water Board. The SAWS' service area currently extends over approximately 561 square miles, making it the largest water purveyor in Bexar County. SAWS serves more than 80% of the water utility customers in Bexar County and provides potable water service to approximately 326,000 customers, which includes residential, commercial, multifamily, industrial, and wholesale accounts. To service its customers, the waterworks system utilizes 24 elevated storage tanks and 35 ground storage reservoirs, of which 9 act as both, with combined storage capacities of 164.28 million gallons. As of 2005, the waterworks system had in place 4,404 miles of distribution mains, ranging in size from 6 to 61 inches in diameter (the majority being between six and 12 inches), and 23,212 fire hydrants distributed evenly throughout the SAWS service area.

Wastewater System. The San Antonio City Council created the City Wastewater System in 1894. A major sewer system expansion program began in 1960 with bond proceeds that provided for new treatment facilities and an enlargement of the wastewater system. In 1970, the City became the Regional Agent of the Texas Commission on Environmental Quality ("TCEQ") (formerly known as the Texas Water Commission and the Texas Water Quality Board). The Regional Agent Boundary encompasses approximately 360 square miles within Bexar County. In 1992, the wastewater system was consolidated with the City's waterworks and recycle water system to form the System.

SAWS serves the residents of the City, 18 governmental entities, and other customers outside the corporate limits of the City. As Regional Agent, SAWS has certain prescribed boundaries that currently cover an area of approximately 403 square miles. SAWS also coordinates with the City for wastewater planning for the City's total planning area, extra-territorial jurisdiction ("ETJ"), of approximately 956 square miles. The population for this planning area is approximately 1.2 million people. SAWS currently provides wastewater services to approximately 354,900 customers.

In addition to the treatment facilities owned by SAWS, there are six privately owned and operated sewage and treatment plants within the San Antonio ETJ.

The wastewater system is composed of approximately 4,607 miles of mains; three major treatment plants (Dos Rios, Leon Creek and Salado Creek); and a smaller treatment plant (Medio Creek). The three major plants are activated sludge facilities and the small plant is an extended aeration plant. SAWS holds Texas Pollutant Discharge Elimination System wastewater discharge permits, issued by the TCEQ for each of these four plants which have a combined treatment capacity of 225.7 million gallons per day. In addition, SAWS operates and maintains several small satellite facilities that vary in number and are temporary, pending completion of interceptor sewers that will connect the flow treated at such facilities to the wastewater system. The permitted flows from the wastewater system's four regional treatment plants represent approximately 98% of the municipal discharges within the ETJ.

Recycling Water System. SAWS is permitted to sell Type I (higher quality) recycled water from its wastewater treatment plants, and has been doing so since 2000. The recycle system is comprised of two north/south transmission lines and an interconnecting line that will be operational in the spring of 2006. Current capacity is 35,000 acre-feet.

Chilled Water and Steam System. SAWS owns and operates eight thermal energy facilities providing chilled water and steam services to governmental and private entities. Two of the facilities, located in the City's downtown area, provide chilled water and/or steam service to 23 customers. Numerous City facilities that include the Convention Center and Alamodome constitute approximately 75% of the downtown system's chilled water and steam annual production requirements. The remaining six thermal energy facilities, owned and operated by SAWS, provide chilled water and steam services to large industrial customers located in the KellyUSA industrial area on the City's west side. Additionally, under a Memorandum of Agreement with the Brooks Development Authority, SAWS provides operational and maintenance services for the Brooks City-Base central thermal energy facility and two small satellite sites. Together, chilled water and steam services produced \$13,370,759 in revenues in fiscal year 2005.

Stormwater System. In September 1997, the City created its Municipal Drainage Utility and established its Municipal Drainage Utility Fund to capture revenues and expenditures for services related to the management of the municipal drainage activity in response to EPA-mandated stormwater runoff and treatment requirements. The City, along with SAWS, has the responsibility, pursuant to the “Authorization to Discharge under the National Pollutant Discharge Elimination System” (the “Permit”), for water quality monitoring and maintenance. The City and SAWS have entered into an interlocal agreement to set forth the specific responsibilities of each regarding the implementation of the requirements under the Permit. The approved annual budget for the SAWS share of program responsibilities for fiscal year 2006 is \$3,447,599, for which SAWS is reimbursed \$3,056,345 from the stormwater utility fee imposed by the City.

Water Supply

Until recently, the City obtained nearly all of its water from the Edwards Aquifer. The Edwards Aquifer lies beneath an area approximately 3,600 square miles in size. Including its recharge zone, it underlies all or part of 13 counties, varying from five to 30 miles in width, and stretching over 175 miles in length, beginning in Bracketville, Kinney County, Texas, in the west and stretching to Kyle, Hays County, Texas, in the east. The Edwards Aquifer receives most of its water from rainfall runoff, rivers, and streams flowing across the 4,400 square miles of drainage basins located above it.

Much of the Edwards Aquifer region consists of agricultural land, but it also includes areas of population ranging from communities with only a few hundred residents to the City, which serves as a home for well over one million residents. The Edwards Aquifer supplies nearly all the water for the municipal, domestic, industrial, commercial, and agricultural needs in this region. Naturally occurring artesian springs, such as the Comal Springs and the San Marcos Springs, are fed by Edwards Aquifer water and are utilized for commercial, municipal, agricultural, and recreational purposes, while at the same time supporting ecological systems containing rare and unique aquatic life.

The Edwards Aquifer is recharged by seepage from streams and by precipitation infiltrating directly into the cavernous, honeycombed, limestone outcroppings in its north and northwestern area. Practically continuous recharge is furnished by spring-fed streams, with stormwater runoff adding additional recharge, as well. The historical annual recharge to the reservoir is approximately 684,700 acre-feet. The average annual recharge over the last four decades is approximately 797,900 acre-feet. The lowest recorded recharge was 43,000 acre-feet in 1956, while the highest was 2,485,000 acre-feet in 1992. Recharge has been increased by the construction of recharge dams over an area of the Edwards Aquifer exposed to the surface known as the recharge zone. The recharge dams, or flood-retarding structures, slows floodwaters and allows much of the water that would have otherwise bypassed the recharge zone to infiltrate the Edwards Aquifer.

Enhancing the City's Water Supply

The City has relied on the Edwards Aquifer as its sole source of water since the 1800s. Beginning in the 1980s and continuing today, however, the management of the water in the Edwards Aquifer has been the subject of intense scrutiny that has led to both extensive litigation and federal and state agency initiation of regulatory action. In 1993, the Texas Legislature adopted the Edwards Aquifer Authority Act, which created a new regulatory agency to manage withdrawals from the Edwards Aquifer and to protect springflows. This agency, known as the Edwards Aquifer Authority (“EAA”), is charged with preserving and protecting the Edwards Aquifer in an eight-county region including all of Uvalde, Medina, and Bexar counties, plus portions of Atascosa, Caldwell, Guadalupe, Comal, and Hays counties.

Based upon population and water demand projections, along with various regulatory and environmental issues, the City recognizes that additional water sources will be required to supplement withdrawals from the Edwards Aquifer to enable the City to meet its long-term water needs.

SAWS is charged with the responsibility of identifying additional water resources for the City and its surrounding areas. New water resource projects range from optimizing the City's current source through conservation measures, to identification and procurement of completely new and independent water sources. These efforts are guided by SAWS long-term water resource planning process, which commenced in 1998 with the

adoption of a 50-year water resource plan. The 1998 plan established mechanisms for formulating and implementing programs to enhance the City's water supply. In October 2000, the City Council created a permanent funding mechanism (the "Water Supply Fee") to be used for water supply development and water quality protection.

The Water Supply Fee is based upon a uniform rate per 100 gallons of water used and is applied to all SAWS customers.

A listing of scheduled water supply fees for years 2001 through 2005 is provided in the following table:

Year	Approved Incremental Charge Per 100 Gallons	Total Approved Charge Per 100 Gallons	Actual Assessment
2001	\$ 0.0358	\$ 0.0358	\$ 0.0358
2002	0.0350	0.0708	0.0708
2003	0.0230	0.0938	0.0844
2004	0.0190	0.1128	0.1100
2005	0.0250	0.1378	0.1378

Source: SAWS, approved by City Council.

On November 17, 2005, the City Council approved the following Water Supply Fee effective January 1, 2006.

Year	Fee Assessed Per 100 Gallons
2006	\$ 0.1487

In August 2005, the 1998 plan was updated to incorporate changes in population forecasts, to reflect the achievements gained through SAWS conservation program, and to identify the best portfolio of water supply projects for meeting San Antonio's future needs. Through this process, SAWS determined that the City's water needs can be met through an array of programs, including a critical period management plan, conservation, reuse, non-Edwards Aquifer groundwater, enhanced recharge capabilities, and aquifer storage and recovery among others. Based on the results of this analysis, the SAWS Board of Trustees approved the 2005 update on August 16, 2005 and directed the SAWS staff to:

- a. Planning Scenario 2: Service as the regional water provided and contact every independent water retailer in Bexar County to see how SAWS can work with them on their long-term water supply needs.
- b. Edwards Supply: Solidify the Edwards Aquifer inventory by converting the approximately 25,000 acre-feet now under lease to permanent ownership, and where possible, seeking an additional 35,000 acre-feet of water rights through either acquisitions or other supply sources.
- c. Recharge Initiatives: Actively participate in the Nueces River Basin Feasibility Study and Cibolo Creek Watershed Feasibility Study. Both studies are on-going and contain local and federal partners. In addition, a continued effort will be made with the Edwards Aquifer Authority to activate the recharge credit rules. This project is further described in the section entitled "Edwards Aquifer Recharge Initiatives."
- d. Brackish Groundwater: Accelerate the brackish groundwater desalination project. This project will assist in diversifying overall supplies in the medium-term. The project will generate up to a 22,000 acre-feet facility, with the potential to offset summer "peaks." This project is further described in the section entitled "Brackish Groundwater Desalination Project."
- e. Regional Carrizo: Accelerate the Regional Carrizo project. Staff should reduce the time for a consultant to perform an independent evaluation of the routing and phasing of this project to three (3)

months, quickly reapply for the initial permit, and continue to pursue leases. This project is further described in the section entitled “Regional Carrizo Aquifer Projects.”

- f. Lower Colorado River Authority-San Antonio Water System: Continue analysis of the feasibility of the Lower Colorado River Authority-San Antonio Water System (“LCRA-SAWS”) project. This project is an important option for meeting long-term water needs. However, renegotiation of the existing contract within the project’s statutory constraints is necessary to more competitively address cost, control, yield, and the timing of the water delivery. This project is further described in the section herein entitled “Lower Colorado River Authority Project.”
- g. Simsboro: Withdraw SAWS’ participation in the Simsboro project. Terminate the existing contract with Alcoa in accordance with its terms and use. With respect to the SAWS-owned water rights, the staff should explore the possible use or disposition of these rights, as opportunity allows.
- h. Lower Guadalupe Water Supply Project: End SAWS’ participation in the Lower Guadalupe Water Supply Project due to the continued uncertainty with the surface water and groundwater regulatory environment of the project area.
- i. Recycle Water: Develop a recycle water business plan. The business plan will address how to increase our contractual usage, obtain additional contracts, and evaluate the implication of an ordinance what would require mandatory connections for certain customer classes. This project is further described in the section entitled “Water Reuse Program.”
- j. Aquifer Storage & Recovery: Maximize SAWS’ Edwards Aquifer storage and the allowable acreage of SAWS’ local Carrizo production. This project is further described in the section entitled “Bexar County Aquifer Storage and Recovery.”
- k. Other Potential Projects: Continue evaluations of other potential water supply projects, including by not limited to: Coastal Desalination, Recharge and Recirculation, Mesa Water Supply Project, Trinity Aquifer, and the Western Edwards Aquifer water projects.

Combined, these actions enable SAWS to provide affordable, diversified, and sufficient water supplies to meet demand in Planning Scenario 2.

Edwards Aquifer Recharge Initiatives

Recharge Dams are structures that retain rainfall runoff water for short periods of time over the Edwards Aquifer Recharge Zone. Recharge dams retain storm runoff and retain it long enough to allow for a larger volume of water to enter into the Edwards Aquifer. During storm events, storm runoff flows at a faster rate than what can be taken by the recharge features located in the stream channels. The recharge dam allows for a longer retention for more water to filter into the Edwards Aquifer thus increasing recharge amounts.

The Nueces, San Antonio, and Guadalupe River Basins are favorable for development of recharge projects. Of the three basins, the Nueces Basin is the most prolific in terms of recharge effectiveness. With assistance from the U.S. Army Corps of Engineers, studies are currently under way within the Cibolo Creek Watershed and the Nueces River Basin. The results of these studies will identify which sites will have the most potential for recharge enhancement. With the recharge structures tentatively identified, the System is planning on a sustained yield of 13,400 acre-feet per year.

Oliver Ranch and BSR Projects

The System reached a milestone in February 2002 with the introduction of the first non-Edwards Aquifer drinking water supply from the Lower Glen Rose/Cow Creek formation of the Trinity Aquifer in northern Bexar County. The System has contracted for delivery of approximately 5,000-acre feet per year of non-Edwards Aquifer 5groundwater from the Trinity Aquifer from two properties located in northern Bexar County. The construction cost to produce and deliver this water supply is approximately \$5.8 million. Initial delivery of water from the Oliver

Ranch project began in February 25, 2002 with BSR production in July 2003. The project was fully operational in June 2004 with the connection of BSR wells 3 and 4 to the System's distribution system.

Western Canyon Project

The System, the San Antonio River Authority ("SARA"), Guadalupe-Blanco River Authority ("GBRA"), and Bexar Metropolitan Water District ("Bexar Met") are working together on the Western Canyon Project for the delivery of water from Canyon Lake. The System will initially receive approximately 8,500 acre-feet per year for service to northern Bexar County. The long-term minimum yield will be 3,950 acre-feet per year. GBRA is required under the contract to divert, treat, and deliver the water to a certain point into the System's delivery system. The permit was issued by the state's regulatory agency, the TCEQ. The project design work has been completed and notice to proceed on construction of various project components took place during the fourth quarter 2004 and first quarter of 2005. Construction of this project is nearing completion, and it is expected that the System will begin receiving water in early 2006.

Brackish Groundwater Desalination Project

The 2005 Update of the System's fifty-year Water Resource Plan includes a recommendation that the System develop a brackish groundwater desalination project. This project involves the development of a moderately sized (up to 22,000 acre-feet) water supply facility with the potential to offset summer "peaks." Hydrologic research on the feasibility of locating this facility in southern Bexar County will begin in December 2005. This analysis will be accompanied by an evaluation of the potential benefit and feasibility of applying innovative procurement methods, such as Design Build Operate and Build Own Operate Transfer strategies to bring this project to on line by 2010.

Regional Carrizo Aquifer Projects

The System is refining plans for delivery and treatment of approximately 20,000 through 56,200 acre-feet of ground water from the Carrizo Aquifer in Gonzales and Wilson Counties. The System is currently undertaking a review process to determine the preferred routing of pipeline associated with the delivery and integration of the Carrizo water into the existing distribution system. Upon completion of this evaluation, which is expected in early 2006, additional construction on this project is scheduled to commence. The project will be developed in phases. The delivery of water from the first phase (22,600 AF) is anticipated in early 2009. Phase II and Phase III are scheduled to be delivered in 2012 and 2016, respectively.

Lower Colorado River Authority Project

The LCRA-SAWS project would conserve and develop up to 330,000 acre-feet of water per year. Of that, approximately 180,000 acre-feet per year of agricultural and other rural water needs would be met in the Colorado basin through conservation of agricultural irrigation water, storage of river water, and supplemental groundwater for agricultural use. Up to 150,000 acre-feet per year of river water would be transferred to the San Antonio area for an eighty-year period.

In February 2001, a Memorandum of Agreement with LCRA outlining the terms for a future binding contract for up to 150,000 acre feet of surface water per year from the Lower Colorado River Basin was signed. That same year, legislation was passed to authorize LCRA to sell water outside its statutory boundary to the System. The System and LCRA have now executed a definitive agreement outlining LCRA's and the System's obligations consistent with the memorandum of Agreement. The System and LCRA are now entering the third year of an estimated seven-year study period to assess the environmental, engineering, and cost impacts.

Bexar County Aquifer Storage and Recovery

An Aquifer Storage and Recovery ("ASR") project involves injecting ground water into an aquifer, storing it and later retrieving it for use. Essentially this is storage that is additionally provided through surface water reservoirs. The System began study of an ASR project in 1996, acquired approximately 3,200 acres in southern Bexar County and has essentially completed the construction of Phase I of the ASR Project. This phase of the

project, with a total cost of approximately \$125 million, gives the System the capability of injecting and recovering 30 million gallons per day of Edwards Aquifer water and integrating it into SAWS' existing distribution system. Phase II of the ASR Project is designed to increase the injection, storage, and recovery capacity of the project to 60 million gallons per day and extend the integration into SAWS' existing distribution system. This phase of the project is currently underway and is anticipated to be complete by the end of 2007.

This project is primarily designed to optimize use of water from the Edwards Aquifer and reduce frequency and duration of critical periods. Additionally, the ASR project may produce "native" groundwater from the project area for use throughout the service areas. In December 2002, the Evergreen Underground Water Conservation District and the System approved an Aquifer Protection and Management Agreement. This agreement ensures operation of the ASR site if the property is annexed in to the district, manages groundwater production, and commits the System to monitoring water levels and mitigation of potential negative impacts. As of December 2005, approximately 17,000 acre-feet of water has been stored in the ASR facility.

Water Reuse Program

The System has developed a water reuse program utilizing high quality effluent from the wastewater treatment process. The System owns the treated effluent from its wastewater treatment plants and has the authority to contract to acquire and to sell non-potable water inside and outside the System's water and wastewater service area. The water reuse system can provide up to 35,000 acre-feet per year for non-potable uses including large scale irrigation and industrial purposes. Once developed to its maximum planned capacity, the System could convert approximately 20% of SAWS current demand for Edwards aquifer water to non-potable uses, thereby making more Edwards water available for potable use. Currently, approximately 19,000 acre-feet of water is under commitment.

In addition to the 35,000 acre-feet per year for irrigation and industrial non-potable uses, the System currently has a contract through 2030 to provide 45,000 acre-feet per year of reuse water to CPS Energy for cooling of electrical generation systems at Braunig and Calaveras lakes. The combined availability of 80,000 acre-feet per year makes this the largest water reuse system in the country. Under the terms of the contract, CPS Energy holds contingent option rights on an additional 10,000 acre-feet of reuse water. These option rights are broken down into two 5,000 acre-feet increments, with the first such option to be exercised no later than June 30, 2007 and the second such option to be exercised no later than June 30, 2011. The revenues derived from the CPS Energy contract have been excluded from the calculation of Gross Revenues and not included in any transfers to the City.

Conservation

Beginning in 1994, the System progressively implemented aggressive water conservation programs, which have reduced total water production and use by 43.2%, from 213 gallons per person per day ("gaped") in 1994 to approximately 130 gaped in 2004. Given these accomplishments, the 2005 update to the System's fifty-year Water Resource Plan set a new goal for conservation that includes the provision that we reduce per capital consumption to 116 gpcd during normal-year conditions and 122 gpcd during dry-year conditions by 2016. This will be accomplished through a variety of means including implementation of the City's water conservation ordinance (Ordinance 100322, passed January 20, 2005), pricing, education, and rebates for water efficient technologies; and system improvements to prevent water loss and other measures.

Indoor Residential Conservation

Indoor residential conservation programs encourage customers to save water inside their homes. A variety of education and rebate incentive programs assist ratepayers in achieving conservation. One example is the Season to Save Community Challenge, which started as an experimental program to test the idea that non-profit organizations would be effective at motivating ratepayers to participate in toilet distribution programs. An incentive is paid to non-profit organizations for finding qualified customers who pick up free toilets during a distribution event. Non-profit groups also receive a bonus for the conservation achieved by customers they helped qualify for the program. The bonus provides incentives for non-profit representatives to ask their participants to install the new toilets quickly.

Another example of the System's conservation program is Plumbers to People, which provides leak repairs and retrofits to qualified low-income homeowner customers. The System, in cooperation with the City of San Antonio's Community Action Division (CAD), qualifies applicants based on the current Federal Assistance Guidelines. Only leaks that result in a loss of potable water are eligible for repair under this program. Water conservation is achieved by quickly repairing leaks that would otherwise continue due to the cost of repairs. Analysis of program costs and water savings indicate that this affordability program is one of our most effective at conserving water at a reasonable cost per unit.

Customers learn about these programs through the System's website, public events, direct mail inserts in bills, paid advertisements and educational materials in popular local periodicals.

Outdoor Residential Conservation

The System's residential outdoor programs focus on the landscape and irrigation practices of homeowners. Outdoor use can account for up to 50% of total residential water use in the summers and average 20% of the water use annually. Education programs help ratepayers understand how following best practices can save water and money.

Irrigation Check-Ups provide the System's ratepayers with a free analysis of their in-ground irrigation system. Trained Conservation Technicians visit homes to review each component of irrigation systems to determine maintenance needs to make suggestions for improving efficiency.

Seasonal Irrigation Program ("SIP") is a free information service provided to customers who want expert advice on how to water their lawns. The irrigation advice is based on evapotranspiration ("ET") data calculated from a local weather station. Horticulture experts from the Texas Cooperative Extension use the ET data to make weekly irrigation recommendations for recommended grass varieties. Customers receive the advice through e-mail, recorded phone message, the local newspaper, a SIP hotline, or the System's web site.

WaterSaver Landscape Rebate guidelines were changed in 2003 to address concerns that the old program was not maximizing water conservation opportunities. Program changes included the requirement that the entire landscape be drought tolerant, a maximum 50% of landscape in grass, and a mandatory irrigation system check if an irrigation system was present. Higher rebates were given to customers who preserved native landscape during home construction or who did not install a permanent irrigation system. An incentive to meet water conservation expectations was included in the program as well. Customers using a reasonable amount of water during the first year after getting their rebate will receive a small nursery gift certificate. This program is marketed through neighborhood associations, local nurseries, the Garden Volunteers of South Texas and through the Greater San Antonio Builder's Association.

Commercial and Industrial Programs

The System has been working closely with commercial customers to help them conserve water for several years. In 1998, the commercial and industrial programs were expanded to include the toilet retrofit rebates previously offered only to residential customers. Water audits and case-by-case rebates for large-scale retrofits are also available. Since 1996, car wash businesses that meet certain conservation criteria are certified and provided a sign to be posted on their place of business. Every year the System presents the WaterSaver Awards to recognize businesses, organizations, and/or individuals that voluntarily initiated water conservation practices.

Agricultural Conservation and Irrigation Efficiency

The System has been successful in developing partners throughout the region as well as with federal agencies through cost-share programs. The amount of \$500,000 for fiscal year has been appropriated by the United States Department of Agriculture ("USDA") for the Edwards Aquifer region to assist landowners with agricultural irrigation efficiencies. The System has partnered with the USDA and farmers to acquire efficient irrigation systems in exchange for Edwards Aquifer water rights. The System is also currently working with the United States Army Corps of Engineers, the Natural Resource Conservation Service and other local sponsors on programs designed to enhance recharge of the Edwards Aquifer through impoundment structures and brush management.

Capital Improvement Plan

The following is a proposed five-year Capital Improvement Program for SAWS. It is the intention of SAWS to fund the program with tax-exempt commercial paper, impact fees, system revenues, and future bond issues. SAWS budgeted the following capital improvement projects during calendar year 2006:

- \$2 million is budgeted for the wastewater treatment program to repair, replace, upgrade, or expand treatment facilities;
- \$28 million is budgeted for the wastewater collection program to fix deteriorated components of the collection system ;
- \$19 million is budgeted to replace sewer and water mains;
- \$44 million is budgeted for the governmental replacement and relocation program;
- \$2 million is budgeted to construct new production facilities; and
- \$79 million is budgeted for water supply development, water treatment, and water transmission projects for new sources of water.

SAWS anticipates the following capital improvement projects for the five fiscal years listed:

	Fiscal Year Ended December 31,					
	2006	2007	2008	2009	2010	Total
Heating and Cooling	\$ 250,000	\$ 950,000	\$ 800,000	\$ 900,000	\$ 300,000	\$ 3,200,000
Water Delivery	51,059,000	52,920,475	54,508,090	56,143,332	57,827,632	272,458,529
Wastewater	65,306,641	63,778,525	65,691,880	67,662,637	69,692,516	332,132,199
Water Supply	82,269,000	73,480,000	101,640,000	88,106,700	98,734,900	444,230,600
Total	<u>\$ 198,884,641</u>	<u>\$ 191,129,000</u>	<u>\$ 222,639,970</u>	<u>\$ 212,812,669</u>	<u>\$ 226,555,048</u>	<u>\$ 1,052,021,328</u>

Source: SAWS. Project Funding Approach

The following table was prepared by SAWS staff based upon information and assumptions it deems reasonable, and shows the projected financing sources to meet the projected capital needs.

	Fiscal Year Ended December 31,					
	2006	2007	2008	2009	2010	Total
Revenues	\$ 26,538,876	\$ 50,262,978	\$ 24,160,707	\$ 28,296,775	\$ 38,560,669	\$ 167,820,005
Impact Fees	16,708,486	9,899,773	10,048,270	10,198,994	10,351,979	57,207,502
Debt Proceeds	155,637,279	130,966,249	188,430,993	174,316,900	177,642,400	826,993,821
Total	<u>\$ 198,884,641</u>	<u>\$ 191,129,000</u>	<u>\$ 222,639,970</u>	<u>\$ 212,812,669</u>	<u>\$ 226,555,048</u>	<u>\$ 1,052,021,328</u>

Source: SAWS.

Recent Financial Transactions

In December 2005, SAWS issued \$298,220,000 “City of San Antonio, Texas Water System Revenue Refunding Bonds, Series 2005”, to advance refund the “City of San Antonio, Texas Water System Revenue and Refunding Bonds, Series 1999” and certain outstanding commercial paper notes.

On May 15, 2006, SAWS refunded \$68,000,000 “City of San Antonio, Texas Water System Revenue Improvement and Refunding Bonds, Series 1996” with the issuance of Tax-Exempt Commercial Paper. The refunding effectively converted the \$68,000,000 of fixed rate bonds into lower coupon variable-rate debt. Total savings from the refunding will depend on future interest rates.

San Antonio Water System Summary of Pledged Revenues for Debt Coverage ¹

	Fiscal Year Ended December 31, 2005	Fiscal Year Ended December 31, 2004	Fiscal Year Ended December 31, 2003	Fiscal Year Ended December 31, 2002	12 Months Ended December 31, 2001 ²
Revenues					
Water System	\$ 93,419,939	\$ 72,888,054	\$ 65,163,910	\$ 58,873,352	\$ 79,451,701
Water Supply	108,045,245	78,546,461	76,044,416	76,167,052	36,684,084
Wastewater System	113,333,959	99,224,713	87,683,794	89,312,338	87,438,542
Chilled Water and Steam	13,370,759	12,027,528	12,193,646	10,871,599	12,899,862
Non Operating Revenues	11,167,861	7,060,677	7,308,979	7,547,353	15,103,714
Adjustments for Pledged Revenues	<u>(6,668,991)</u>	<u>(5,437,557)</u>	<u>(5,591,341)</u>	<u>(7,583,370)</u>	<u>(5,911,934)</u>
Total Revenues	<u>\$332,668,772</u>	<u>\$264,309,876</u>	<u>\$242,803,404</u>	<u>\$235,188,324</u>	<u>\$225,665,969</u>
Maintenance and Operating Expenses	<u>\$173,489,890</u>	<u>\$153,859,964</u>	<u>\$152,742,554</u>	<u>\$138,212,615</u>	<u>\$134,616,252</u>
Net Available for Debt Service	<u>\$159,178,882</u>	<u>\$110,449,912</u>	<u>\$ 90,060,850</u>	<u>\$ 96,975,709</u>	<u>\$ 91,049,717</u>
Maximum Annual Debt Service Requirements - Total Debt ³	\$ 94,992,353	\$ 84,941,122	\$ 76,075,114	\$ 66,267,591	\$ 65,767,934
Maximum Annual Debt Service Requirements - Senior Lien Debt ³	\$ 78,372,649	\$ 67,203,188	\$ 61,511,375	\$ 61,511,375	\$ 55,236,354
Coverage of Total Debt	1.68 X	1.30 X	1.18 X	1.46 X	1.38 X
Coverage of Senior Lien Debt	2.03 X	1.64 X	1.46 X	1.58 X	1.65 X

¹ Unaudited.

² On April 3, 2001, the SAWS Board approved the changing of the fiscal year from a year-end of May 31 to December 31. Report is for the twelve (12) months ending December 31, 2001.

³ As of the end of the fiscal year shown, excludes Tax Exempt Commercial Paper.

Source: SAWS.

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The Airport System

The City's Airport System is described in detail in the body of this Official Statement.

* * *

APPENDIX B

EXCERPTS FROM ORDINANCE

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APPENDIX B

EXCERPTS FROM THE MASTER ORDINANCE AND THE EIGHTH SUPPLEMENT

THE FOLLOWING CAPITALIZED TERMS ARE DEFINED IN THE MASTER ORDINANCE AND ARE APPLICABLE TO THE EIGHTH SUPPLEMENT

[Note: The term "Pre-2001 Parity Obligations" used in this Appendix refers to airport revenue bonds issued by the City prior to the adoption of the Master Ordinance and which were secured by a first lien on and pledge of the Gross Revenues of the Airport System on parity with all Parity Obligations issued pursuant to the Master Ordinance. Upon the issuance of the Series 2006 Bonds, no Pre-2001 Parity Obligations will remain outstanding.]

"Account" means any account created, established and maintained under the terms of any Supplement.

"Accountant" means a nationally recognized independent certified public accountant, or an independent firm of certified public accountants.

"Additional Parity Obligations" shall mean the additional parity revenue obligations which the City reserves the right to issue in the future as provided in Section 17 of the Master Ordinance.

"Airport System" means and includes the City of San Antonio International Airport and Stinson Municipal Airport, as each now exists, and all land, buildings, structures, equipment, and facilities pertaining thereto, together with all future improvements, extensions, enlargements, and additions thereto, and replacements thereof, and all other airport facilities of the City acquired or constructed with funds from any source, including the issuance of Parity Obligations; provided, however, for the purpose of providing further clarification, the term "Airport System" shall not include Industrial Properties and Special Facilities Properties.

"Airport Consultant" means an airport consultant or airport consultant firm or corporation having a wide and favorable reputation for skill and experience with respect to the operation and maintenance of airports, in recommending rental and other charges for use of airport facilities and in projecting revenues to be derived from the operation of airports, and not a full time employee of the City.

"Annual Budget" means the annual budget of the Airport System (which may be included in the City's general annual budget), as amended and supplemented, adopted or in effect for a particular Fiscal Year.

"Annual Debt Service Requirements" means, for any Fiscal Year, the principal of and interest on all Parity Obligations coming due at Maturity or Stated Maturity (or that could come due on demand of the owner thereof other than by acceleration or other demand conditioned upon default by the City on such Debt, or be payable in respect of any required purchase of such Debt by the City) in such Fiscal Year, less and except any such principal or interest for the payment of which provision has been made by (i) appropriating for such purpose amounts sufficient to provide for the full and timely payment of such interest or principal either from proceeds of bonds, notes or other obligations, from interest earned or to be earned thereon, from Airport System funds other than Gross Revenues, or from any combination of such sources and (ii) depositing such amounts (except in the case of interest to be earned, which shall be deposited as received) into a dedicated Fund or Account, the proceeds of which are required to be transferred as needed into the Bond Fund or directly to the Paying Agent for such Parity Obligations; and, for such purposes, any one or more of the following rules shall apply at the election of the City:

(1) Committed Take Out. If the City has entered into a Credit Agreement constituting a binding commitment within normal commercial practice, from any bank, savings and loan association, insurance company, or similar institution to discharge any of its Funded Debt at its Stated Maturity (or, if due on demand, at any date on which demand may be made) or to purchase any of its Funded Debt at any date on which such Debt is subject to required purchase, all under arrangements whereby the City's obligation to repay the amounts advanced for such discharge or purchase constitutes Funded Debt, then the portion of the Funded Debt committed to be discharged or purchased shall be excluded from such calculation and the principal of and interest on the Funded Debt incurred for such discharging or purchase that would be due in the Fiscal Year for which the calculation is being made,

if incurred at the Stated Maturity or purchase date of the Funded Debt to be discharged or purchased, shall be added;

(2) Balloon Debt. If the principal (including the accretion of interest resulting from original issue discount or compounding of interest) of any series or issue of Funded Debt due (or payable in respect of any required purchase of such Funded Debt by the City) in any Fiscal Year either is equal to at least 25% of the total principal (including the accretion of interest resulting from original issue discount or compounding of interest) of such Funded Debt or exceeds by more than 50% the greatest amount of principal of such series or issue of Funded Debt due in any preceding or succeeding Fiscal Year (such principal due in such Fiscal Year for such series or issue of Funded Debt being referred to herein and throughout this Exhibit A as "Balloon Debt"), the amount of principal of such Balloon Debt taken into account during any Fiscal Year shall be equal to the debt service calculated using the original principal amount of such Balloon Debt amortized over the Term of Issue on a level debt service basis at an assumed interest rate equal to the rate borne by such Balloon Debt on the date of calculation;

(3) Consent Sinking Fund. In the case of Balloon Debt, if a Designated Financial Officer shall deliver to the City a certificate providing for the retirement of (and the instrument creating such Balloon Debt shall permit the retirement of), or for the accumulation of a sinking fund for (and the instrument creating such Balloon Debt shall permit the accumulation of a sinking fund for), such Balloon Debt according to a fixed schedule stated in such certificate ending on or before the Fiscal Year in which such principal (and premium, if any) is due, then the principal of (and, in the case of retirement, or to the extent provided for by the sinking fund accumulation, the premium, if any, and interest and other debt service charges on) such Balloon Debt shall be computed as if the same were due in accordance with such schedule, provided that this clause (3) shall apply only to Balloon Debt for which the installments previously scheduled have been paid or deposited to the sinking fund established with respect to such Debt on or before the times required by such schedule; and provided further that this clause (3) shall not apply where the City has elected to apply the rule set forth in clause (2) above;

(4) Prepaid Debt. Principal of and interest on Parity Obligations, or portions thereof, shall not be included in the computation of the Annual Debt Service Requirements for any Fiscal Year for which such principal or interest are payable from funds on deposit or set aside in trust for the payment thereof at the time of such calculations (including without limitation capitalized interest and accrued interest so deposited or set aside in trust) with a financial institution acting as fiduciary with respect to the payment of such Debt;

(5) Variable Rate.

(A) Except as hereinafter provided in this subparagraph, the rate of interest on Variable Rate Obligations then proposed to be issued shall be deemed to be the average for the then immediately preceding five years of the BMA Index, plus 20 basis points; provided, however, that (i) if, after the issuance of the Variable Rate Obligations then proposed to be issued, more than 20% of the aggregate of the Parity Obligations Outstanding will bear interest at a variable rate and (ii) any Parity Obligation is then insured by a Bond Insurer, the rate of interest on Variable Rate Obligations then proposed to be issued shall be deemed to be the greater of (x) the most recently announced 30-year Revenue Bond Index published by The Bond Buyer, a financial journal published, as of the date the Master Ordinance was adopted, in The City of New York, New York, (y) the rate of interest then borne by any Variable Rate Obligations then Outstanding, and (z) 1.25 times the average variable rate borne by any Variable Rate Obligations then Outstanding during the then immediately preceding twelve-month period, or if no Variable Rate Obligations are then Outstanding, 1.25 times the average variable rate for similarly rated obligations with comparable maturities during the then immediately preceding twelve-month period, and

(B) Except as hereinafter provided in this subparagraph, the rate of interest on Variable Rate Obligations outstanding at the time of such calculation shall be deemed to be the lesser of (i) the then current per annum rate of interest borne by such Variable Rate Obligations or (ii) the average per annum rate of interest borne by such Variable Rate Obligations during the then immediately preceding twelve-month period; provided, however,

that for any period during which (a) more than 20% of the aggregate of the Parity Obligations then Outstanding bear interest at a variable rate and (b) any Parity Obligation is then insured by a Bond Insurer, the rate of interest on such Variable Rate Obligations shall be the greater of (x) the most recently announced 30 year Revenue Bond Index published by The Bond Buyer, a financial journal published, as of the date the Master Ordinance was adopted, in The City of New York, New York, (y) the rate of interest then in effect with respect to such Variable Rate Obligations in accordance with their terms, and (z) 1.25 times the average variable rate borne by such Variable Rate Obligations during the then immediately preceding twelve-month period;

(6) Credit Agreement Payments. If the City has entered into a Credit Agreement in connection with an issue of Debt, payments due under the Credit Agreement (other than payments made by the City in connection with the termination or unwinding of a Credit Agreement), from either the City or the Credit Provider, shall be included in such calculation except to the extent that the payments are already taken into account under (1) through (5) above and any payments otherwise included above under (1) through (5) which are to be replaced by payments under a Credit Agreement, from either the City or the Credit Provider, shall be excluded from such calculation. With respect to any calculation of historic data, only those payments actually made in the subject period shall be taken into account in making such calculation and, with respect to prospective calculations, only those payments reasonably expected to be made in the subject period shall be taken into account in making the calculation.

"Average Annual Debt Service Requirements" means, as of the time of computation, the aggregate of the Annual Debt Service Requirement for each Fiscal Year that Parity Obligations are Outstanding from the date of such computation, divided by the number of Fiscal Years remaining to the final Stated Maturity of such Parity Obligations.

"Aviation Director" means the director of the City's Department of Aviation, or the successor or person acting in such capacity.

"BMA Index" means the "high grade" seven-day index made available by The Bond Markets Association of New York, New York, or any successor thereto, based upon 30-day yield evaluation at par of bonds, the interest income on which is excludable from gross income of the recipients thereof for federal income tax purposes. In the event that neither The Bond Markets Association nor any successor thereto makes available an index conforming to the requirements of the preceding sentence, the term "BMA Index" shall mean an index determined by the City based upon the rate for bonds rated in the highest short-term rating category by Moody's and Standard & Poor's, the interest income on which is excludable from gross income of the recipients thereof for federal income tax purposes, in respect of issuers most closely resembling the "high grade" component issuers selected by "BMA Index".

"Bond Counsel" means an independent attorney or firm of attorneys selected by the City whose opinions respecting the legality or validity of securities issued by or on behalf of states or political subdivisions thereof are nationally recognized.

"Bond Fund" means the "City of San Antonio General Airport Revenue Parity Obligations Bond Fund", the existence of which is confirmed in Section 5(b), and is further described in Section 7, of the Master Ordinance.

"Bond Insurer" means any insurance company insuring payment of municipal bonds and other similar obligations if such bond or obligations so insured by it are eligible for a rating by a Credit Rating Agency, at the time of the delivery of a Municipal Bond Insurance Policy, in one of its two highest rating categories.

"Bond Reserve Fund" means the "City of San Antonio General Airport Revenue Parity Obligations Reserve Fund", the existence of which is confirmed in Section 5(c), and is further described in Section 8, of the Master Ordinance.

"Business Day" means any day other than a Saturday, a Sunday or a day on which the City or the city in which the payment office of the Paying Agent is located is authorized by law to remain closed and is closed.

"Capital Improvement Fund" means the "City of San Antonio Capital Improvement Fund", the existence of which is confirmed in Section 5(e), and is further described in Section 12, of the Master Ordinance.

"Capital Improvements" means improvements, extensions and additions to the Airport System (other than Special Facilities) that are properly chargeable to capital account by generally accepted accounting practice and includes, without limitations, equipment and rolling stock so chargeable and real estate (and easements and other interests therein) on, under or over which any such improvements, extensions or additions are, or are proposed to be, located.

"Chapter 1371" means Chapter 1371, Texas Government Code.

"Chapter 2256" means Chapter 2256, Texas Government Code.

"City" or **"Issuer"** mean the City of San Antonio, Texas.

"Code" means the Internal Revenue Code of 1986, as amended, any successor federal income tax laws or any regulations promulgated or rulings published pursuant thereto.

"Completion Obligations" means any bonds, notes or other obligations issued or incurred by the City for the purpose of completing any Capital Improvement for which Parity Obligations have previously been issued or incurred by the City, as described in Section 17(c) of the Master Ordinance.

"Credit Agreement" means, collectively, a loan agreement, revolving credit agreement, agreement establishing a line of credit, letter of credit, reimbursement agreement, insurance contract, commitments to purchase Parity Obligations, purchase or sale agreements, interest rate swap agreements, or commitments or other contracts or agreements authorized, recognized and approved by the City as a Credit Agreement in connection with the authorization, issuance, security, or payment of Parity Obligations and on a parity therewith.

"Credit Facility" means (i) a policy of insurance or a surety bond, issued by a Bond Insurer or an issuer of policies of insurance insuring the timely payment of debt service on governmental obligations, provided that a Credit Rating Agency having an outstanding rating on Parity Obligations would rate the Parity Obligations fully insured by a standard policy issued by the issuer in its highest generic rating category for such obligations; and (ii) a letter of credit or line of credit issued by any financial institution, provided that a Credit Rating Agency having an outstanding rating on the Parity Obligations would rate the Parity Obligations in its two highest generic rating categories for such obligations if the letter of credit or line of credit proposed to be issued by such financial institution secured the timely payment of the entire principal amount of the Parity Obligations and the interest thereon.

"Credit Provider" means any bank, financial institution, insurance company, surety bond provider, or other institution which provides, executes, issues, or otherwise is a party to or provider of a Credit Agreement or Credit Facility.

"Credit Rating Agency" means (a) Fitch, (b) Moody's, (c) Standard & Poor's, (d) any successor to any of the foregoing by merger, consolidation or otherwise, and (e) any other nationally recognized municipal securities rating service from whom the City seeks and obtains a rating on any issue or series of Parity Obligations.

"Debt" of the City payable from Gross Revenues or Net Revenues means all:

(1) indebtedness incurred or assumed by the City for borrowed money (including indebtedness arising under Credit Agreements) and all other financing obligations of the City issued or incurred for the Airport System that, in accordance with generally accepted accounting principles, are shown on the liability side of a balance sheet; and

(2) all other indebtedness (other than indebtedness otherwise treated as Debt hereunder) for borrowed money or for the acquisition, construction, or improvement of property or capitalized lease obligations at or for the Airport System that is guaranteed, directly or indirectly, in any manner by the City, or that is in effect guaranteed, directly or indirectly, by the City through an agreement, contingent or otherwise, to purchase any such indebtedness or to advance or supply funds for the payment or purchase of any such indebtedness or to purchase property or services primarily for the purpose of enabling the debtor or seller to make payment of such indebtedness, or to assure the owner of the indebtedness against loss, or to supply funds to or in any other manner invest in the debtor (including any agreement to pay for property or services irrespective of whether or not such property is delivered or such services are rendered), or otherwise.

For the purpose of determining the "Debt" payable from the Gross Revenues, there shall be excluded any particular Debt if, upon or prior to the Maturity thereof, there shall have been deposited with the proper depository (a) in trust the necessary funds (or investments that will provide sufficient funds, if permitted by the instrument creating such Debt) for the payment, redemption, or satisfaction of such Debt or (b) evidence of such Debt deposited for cancellation; and thereafter it shall not be considered Debt. Except as may be otherwise provided above, no item shall be considered Debt unless such item constitutes indebtedness under generally accepted accounting principles applied on a basis consistent with the financial statements of the City in prior Fiscal Years.

"Designated Financial Officer" means the City Manager, the Director of Finance, or such other financial or accounting official of the City so designated by the governing body of the City.

"Eligible Investments" means (i) those investments in which the City is now or hereafter authorized by law, including, but not limited to, Chapter 2256, to purchase, sell and invest its funds and funds under its control and (ii) any other investments not specifically authorized by Chapter 2256 but which may be designated by the terms of a Supplement as Eligible Investments under authority granted by Chapter 1371.

"Federal Payments" means those funds received by the City from the federal government or any agency thereof as payments for the use of any facilities or services of the Airport System.

"Fiscal Year" means the successive twelve-month period designated by the City as its fiscal year of the City, which currently ends on September 30 of each calendar year.

"Fitch" means Fitch, Inc.

"Fund" means any fund created, established and maintained under the terms of the Master Ordinance and any Supplement.

"Funded Debt" of the Airport System means all Parity Obligations (and, for purposes of Section 17(d) of the Master Ordinance, all Subordinated Debt) created or assumed by the City and payable from Gross Revenues that mature by their terms (in the absence of the exercise of any earlier right of demand), or that are renewable at the option of the City to a date, more than one year after the original creation or assumption of such Debt by the City.

"Gross Revenues" means all of the revenues and income of every nature and from whatever source derived by the City (but excluding grants and donations for capital purposes) from the operation and/or ownership of the Airport System, including the investment income from the investment or deposit of money in each Fund (except the Construction Fund, any Rebate Fund, and interest earnings required to be deposited to any Rebate Fund) created, maintained or confirmed by the Master Ordinance; provided, however, that if the net rent (excluding ground rent) from any Special Facilities Lease is pledged to the payment of principal, interest, reserve, or other requirements in connection with revenue bonds issued by the City to provide Special Facilities for the Airport System for the lessee (or in connection with obligations issued to refund said revenue bonds) the amount of such net rent so pledged and actually used to pay such requirements shall not constitute or be considered as Gross Revenues, but all ground rent, and any net rent in excess of the amounts so pledged and used, shall be deposited in the Revenue Fund described in the Master Ordinance. Without limiting the generality of the foregoing, the term *Gross Revenues* shall include all landing fees and charges, ground rentals, space rentals in buildings and all charges made to concessionaires, and all revenues of any nature derived from contracts or use agreements with airlines and other users of the Airport System and its facilities; provided, however, that the term Gross Revenues shall not include any "passenger facility charges" described substantially in the manner provided in the "Aviation Safety and Capacity Expansion Act of 1990" (P.L. 101-508, Title IX) or the "Aviation Investment and Reform Act for the 21st Century" enacted by Congress in the year 2000, or other similar federal laws and the rules and regulations promulgated thereby, or any other similar charges that may be imposed pursuant to federal law.

"Holder" or "Bondholder" or "owner" means the registered owner of any Parity Obligation registered as to ownership and the holder of any Parity Obligation payable to bearer, or as otherwise provided for in a Supplement.

"Industrial Properties" means (a) the real and personal properties situated at and around the Airport System which are owned by the City and (i) leased to industrial or commercial tenants engaged in activities which are unrelated to the City's public airport operations, or (ii) held by the City for future industrial and commercial development, and (b) any other real or personal property now owned or hereafter acquired by the City which is unrelated to the City's public airport operations.

"Master Ordinance" means Ordinance No. 93789 of the City, adopted on April 19, 2001, which established the General Airport Revenue Bond Financing Program.

"Maturity" when used with respect to any Debt means the date on which the principal of such Debt or any installment thereof becomes due and payable as therein provided, whether at the Stated Maturity thereof or by declaration of acceleration, call for redemption, or otherwise.

"Moody's" means Moody's Investors Service, Inc.

"Net Revenues" means the Gross Revenues after deducting Operation and Maintenance Expenses.

"Operation and Maintenance Expenses" means the reasonable and necessary current expenses of the City paid or accrued in administering, operating, maintaining, and repairing the Airport System. Without limiting the generality of the foregoing, the term "Operation and Maintenance Expenses" shall include all costs directly related to the Airport System, that is, (1) collecting Gross Revenues and of making any refunds therefrom lawfully due others; (2) engineering, audit reports, legal, and other overhead expenses directly related to its administration, operation, maintenance, and repair; (3) salaries, wages and other compensation of officers and employees, and payments to pension, retirement, health and hospitalization funds and other insurance, including self-insurance for the foregoing (which shall not exceed a level comparable to airports of a similar size and character); (4) costs of routine repairs, replacements, renewals, and alterations not constituting a capital improvement, occurring in the usual course of business; (5) utility services; (6) expenses of general administrative overhead of the City allocable to the Airport System; (7) equipment, materials and supplies used in the ordinary course of business not constituting a capital improvement, including ordinary and current rentals of equipment or other property; (8) fidelity bonds, or a properly allocable share of the premium of any blanket bond, pertaining to the Airport System or Gross Revenues or any other moneys held hereunder or required hereby to be held or deposited hereunder; and (9) costs of carrying out the provisions of the Master Ordinance, including paying agent's fees and expenses; costs of insurance required hereby, or a properly allocable share of any premium of any blanket policy pertaining to the Airport System or Gross Revenues, and costs of recording, mailing, and publication. To provide further clarification, Operation and Maintenance Expenses shall not include the following: (1) any allowances for depreciation; (2) costs of capital improvements; (3) reserves for major capital improvements, Airport System operations, maintenance or repair; (4) any allowances for redemption of, or payment of interest or premium on, Debt; (5) any liabilities incurred in acquiring or improving properties of the Airport; (6) expenses of lessees under Special Facilities Leases and operation and maintenance expenses pertaining to Special Facilities to the extent that they are required to be paid by such lessees pursuant to the terms of the Special Facilities Leases; (7) liabilities based upon the City's negligence or other ground not based on contract; and (8) to the extent Federal Payments may not be included as Gross Revenues, an amount of expenses that would otherwise constitute Operation and Maintenance Expenses for such period equal to the Federal Payments for such period.

"Outstanding" when used with respect to Parity Obligations means, as of the date of determination, all Parity Obligations theretofore delivered under the Master Ordinance and any Supplement, except:

(1) Parity Obligations theretofore cancelled and delivered to the City or delivered to the Paying Agent or the Registrar for cancellation;

(2) Parity Obligations deemed paid pursuant to the defeasance provisions as set forth in any Supplement;

(3) Parity Obligations upon transfer of or in exchange for and in lieu of which other Parity Obligations have been authenticated and delivered pursuant to the Master Ordinance and any Supplement; and

(4) Parity Obligations under which the obligations of the City have been released, discharged, or extinguished in accordance with the terms thereof;

provided, that, unless the same is acquired for purposes of cancellation, Parity Obligations owned by the City shall be deemed to be Outstanding as though it was owned by any other owner.

"Outstanding Principal Amount" means, with respect to all Parity Obligations or to a series of Parity Obligations, the outstanding and unpaid principal amount of such Parity Obligations paying interest on a current basis and the outstanding and unpaid principal and compounded interest on such Parity Obligations paying accrued, accreted, or compounded interest only at maturity as of any "Record Date" established by a Registrar in a Supplement or in

connection with a proposed amendment of the Master Ordinance. For purposes of this definition, payment obligations of the City under the terms of a Credit Agreement that is treated as a Parity Obligation shall be treated as outstanding and unpaid principal.

"Parity Obligations" means all Outstanding Pre-2001 Parity Obligations, any Additional Parity Obligations issued pursuant to a Supplement and in accordance with Section 17 of the Master Ordinance, and all other Debt of the City which may be issued, incurred or assumed in accordance with the terms of the Master Ordinance and a Supplement and which is secured by a first lien on and pledge of the Gross Revenues.

"Paying Agent" means each entity designated in a Supplement as the place of payment of a series or issue of Parity Obligations.

"Person" means any natural person, firm, partnership, association, corporation, or public body.

"Registrar" means each entity designated in a Supplement as the registrar of a series or issue of Parity Obligations.

"Required Reserve Amount" means an amount of money and investments equal in market value to the Average Annual Debt Service Requirements of all Parity Obligations at any time Outstanding.

"Reserve Fund Obligations" means cash, Eligible Investments, any Credit Facility, or any combination of the foregoing.

"Revenue Fund" means the "City of San Antonio Airport System Revenue Fund", the existence of which is confirmed in Section 5a, and is further described in Section 6 of, the Master Ordinance.

"Special Contingency Reserve Fund" means the "City of San Antonio Parity Obligations Special Contingency Reserve Fund", the existence of which is confirmed in Section 5(d), and is further described in Section 11, of the Master Ordinance.

"Special Facilities" and **"Special Facilities Properties"** mean structures, hangars, aircraft overhaul, maintenance or repair shops, heliports, hotels, storage facilities, garages, inflight kitchens, training facilities and any and all other facilities and appurtenances being a part of or related to the Airport System the cost of the construction or other acquisitions of which is financed with the proceeds of Special Facilities Debt. Upon the retirement of Special Facilities Debt, the City may declare such facilities financed with such Special Facilities Debt to be within the meaning of "Airport System," as hereinabove defined.

"Special Facilities Debt" means those bonds, notes or other obligations from time to time hereafter issued or incurred by or on behalf of the City pursuant to Section 17(d) of the Master Ordinance.

"Special Facilities Lease" means any lease or agreement, howsoever denominated, pursuant to which a Special Facility is leased by or on behalf of the City to the lessee in consideration for which the lessee agrees to pay (i) all debt service on the Special Facilities Debt issued to finance the Special Facility (which payments are pledged to secure the Special Facilities Debt) and (ii) the operation and maintenance expenses of the Special Facility.

"Standard & Poor's" means Standard & Poor's Rating Services, a division of The McGraw-Hill Companies.

"Stated Maturity" means, when used with respect to any Debt or any installment of interest thereon, any date specified in the instrument evidencing or authorizing such Debt or such installment of interest as a fixed date on which the principal of such Debt or any installment thereof or the fixed date on which such installment of interest is due and payable.

"Subordinated Debt" means any Debt which expressly provides that all payments thereon shall be subordinated to the timely payment of all Parity Obligations then Outstanding or subsequently issued.

"Subordinated Debt Fund" means the "City of San Antonio General Airport Revenue Subordinated Debt Fund" established pursuant to Section 10 of the Master Ordinance.

"Supplement" or "Supplemental Ordinance" mean an ordinance supplemental to, and authorized and executed pursuant to the terms of, the Master Ordinance.

"Tax-Exempt Debt" means Debt interest on which is excludable from the gross income of the Holder for federal income tax purposes under section 103 of the Code.

"Term of Issue" means with respect to any Balloon Debt, a period of time equal to the greater of (i) the period of time commencing on the date of issuance of such Balloon Debt and ending on the final maturity date of such Balloon Debt or (ii) twenty-five years.

"Variable Rate Obligations" means Parity Obligations that bear interest at a rate per annum which is subject to adjustment so that the actual rate of interest is not ascertainable at the time such Parity Obligations are issued; provided, however, that upon the conversion of the rate of interest on a Variable Rate Obligation to a fixed rate of interest (whether or not the interest rate thereon is subject to conversion back to a variable rate of interest), such Parity Obligation shall not be treated as a "Variable Rate Obligation" for so long as such Parity Obligation bears interest at a fixed rate.

THE FOLLOWING SECTIONS 2 THROUGH 10 AND 12 THROUGH 20 APPEAR IN THE MASTER ORDINANCE:

SECTION 2. SECURITY AND PLEDGE. (a) ***First Lien on Gross Revenues.*** The Parity Obligations are and shall be secured by and payable from a first lien on and pledge of the Gross Revenues, in accordance with the terms of this Master Ordinance, any Supplement and, with respect to the Pre-2001 Parity Obligations only, the ordinances of the City which authorized the issuance of such Pre-2001 Parity Obligations; and the Gross Revenues are further pledged to the establishment and maintenance of the Bond Fund, Bond Reserve Fund and the other Funds and Accounts (excluding any Rebate Fund) provided in accordance with the terms of this Master Ordinance and any Supplement. The Parity Obligations are and will be secured by and payable only from the Gross Revenues, and are and will not be secured by or payable from a mortgage or deed of trust on any properties, whether real, personal, or mixed, constituting any portion of the Airport System. The owners of the Parity Obligations shall never have the right to demand payment out of funds raised or to be raised by taxation, or from any source other than specified in this Master Ordinance or any Supplement.

(b) ***Ability to Pledge Other Revenues.*** In addition to securing all Parity Obligations with a first lien on and pledge of the Gross Revenues, the City reserves the right to further secure the payment of any Parity Obligations, or to secure the payment of any Debt (including Subordinated Debt) or other short term or long term indebtedness incurred by the City relating to the Airport System with a lien on and pledge of any other lawfully available revenues of the Airport System, including, but not limited to, all or a portion of "passenger facility charges" authorized to be levied and collected by the City in accordance with the provisions of the "*Aviation Safety and Capacity Expansion Act of 1990*" (P.L. 101-508, Title IX) or the "*Aviation Investment and Reform Act for the 21st Century*" enacted by Congress in the year 2000, or other similar federal laws and the rules and regulations promulgated thereby, or any other similar charges that may be imposed pursuant to federal law, all pursuant to the Supplement which authorizes the issuance of such Parity Obligations or Subordinated Debt.

SECTION 3. RATE COVENANT; RECOMMENDATION OF AIRPORT CONSULTANT. (a) ***Rate Covenant.*** The City covenants and agrees with the holders of all Parity Obligations, as follows:

(1) It will at all times fix, maintain, enforce, charge, and collect rates, fees, charges, and amounts for the use, occupancy, services, facilities, and operation of the Airport System which will produce in each Fiscal Year Gross Revenues at least sufficient: (A) to pay all Operation and Maintenance Expenses during each Fiscal Year, and also (B) to provide an amount equal to 1.25 times the Annual Debt Service Requirements during each Fiscal Year on all then Outstanding Parity Obligations.

(2) If the Airport System should become legally liable for any other obligations or indebtedness, the City shall fix, maintain, enforce, charge, and collect additional rates, fees, charges, and amounts for the use, occupancy, services, facilities and operation of the Airport System sufficient to establish and maintain funds for the payment thereof.

(b) ***Recommendation of Airport Consultant.*** If the Gross Revenues in any Fiscal Year are less than the amounts specified above, the City, promptly upon receipt of the annual audit for such Fiscal Year, shall request an Airport Consultant to make its recommendations, if any, as to a revision of the City's rentals, rates, fees and other charges, its Operation and Maintenance Expenses, or the method of operation of the Airport System in order to satisfy as quickly as practicable the foregoing rate covenant. Copies of such request and the recommendation of the Airport

Consultant, if any, shall be filed with the City Clerk. So long as the City substantially complies in a timely fashion with the recommendation of the Airport Consultant, the City will not be deemed to have defaulted in the performance of its duties under this Master Ordinance even if the resulting Gross Revenues are not sufficient to be in compliance with the rate covenant set forth above, so long as the Annual Debt Service Requirements on the Parity Obligations are paid when due.

SECTION 4. GENERAL COVENANTS. While any Parity Obligation is Outstanding, the City further covenants and agrees that in accordance with and to the extent required or permitted by law:

(a) **Performance.** The City will faithfully perform at all times any and all covenants, undertakings, stipulations, and provisions contained in this Master Ordinance and any Supplement; it will promptly pay or cause to be paid the principal amount of and interest on every Parity Obligation, on the dates and in the places and manner prescribed in a Supplement and such Parity Obligations; and it will, at the time and in the manner prescribed, deposit or cause to be deposited the amounts required to be deposited into the Funds and Accounts as provided in accordance with this Master Ordinance and any Supplement.

(b) **City's Legal Authority.** The City is a duly created and existing home rule municipality and is duly authorized under the laws of the State of Texas to issue and incur Parity Obligations; that all action on its part to issue or incur Parity Obligations shall have been duly and effectively taken, and that the Parity Obligations in the hands of the owners thereof are and will be valid and enforceable special obligations of the City in accordance with their terms.

(c) **Title.** It has or will obtain lawful title, whether such title is in fee or lesser interest, to the lands, buildings, structures and facilities constituting the Airport System, that it warrants that it will defend the title to all the aforesaid lands, buildings, structures and facilities, and every part thereof, against the claims and demands of all Persons whomsoever, that it is lawfully qualified to pledge the Gross Revenues to the payment of the Parity Obligations in the manner prescribed herein, and has lawfully exercised such rights.

(d) **Liens.** It will from time to time and before the same become delinquent pay and discharge all taxes, assessments and governmental charges, if any, which shall be lawfully imposed upon it, or the Airport System; it will pay all lawful claims for rents, royalties, labor, materials and supplies which if unpaid might by law become a lien or charge thereon, the lien of which would be prior to or interfere with the liens granted in accordance with the terms of this Master Ordinance, so that the priority of the liens granted in accordance with the terms of this Master Ordinance shall be fully preserved in the manner provided herein, and it will not create or suffer to be created any mechanic's, laborer's, materialman's or other lien or charge which might or could be prior to the liens granted in accordance with the terms of this Master Ordinance, or do or suffer any matter or thing whereby the liens granted in accordance with the terms of this Master Ordinance might or could be impaired; provided, however, that no such tax, assessment or charge, and that no such claims which might be used as the basis of a mechanic's, laborer's, materialman's or other lien or charge, shall be required to be paid so long as the validity of the same shall be contested in good faith by the City.

(e) **Operation of Airport System.** The City will continuously and efficiently operate the Airport System and shall maintain the Airport System in good condition, repair, and working order, all at reasonable cost. The City will not supply space, services, or privileges at the Airport System without making commensurate charges therefor, except to the extent actually required by law in connection with Federal and State authorities.

(f) **Further Encumbrance.** The City will not additionally encumber the Gross Revenues or the Net Revenues in any manner, except as permitted in this Master Ordinance and any Supplement in connection with Parity Obligations, unless said encumbrance is made junior and subordinate in all respects to the liens, pledges, covenants and agreements of this Master Ordinance and any Supplement; but the right of the City to issue or incur Subordinated Debt payable in whole or in part from a subordinate lien on the Net Revenues is specifically recognized and retained.

(g) **Sale, Lease, or Encumbrance of Airport System.** Except for the use of the Airport System or services pertaining thereto in the normal course of business, neither all nor a substantial part of the Airport System shall be sold, leased, mortgaged, pledged, encumbered, alienated, or otherwise disposed of until all Parity Obligations have been paid in full, or unless provision has been made therefor, and the City shall not dispose of its title to the Airport System or to any useful part thereof, including, without limitation, any property necessary to the operation and use of the Airport System, other than (i) in connection with the execution of leases, licenses, easements, or other agreements in connection with the operation of the Airport System by the City, or in connection with any Special Facilities thereat, (ii) in connection with any pledges of and liens on revenues derived from the operation and use of the Airport System or any part thereof, or any Special Facilities pertaining thereto, for the payment of Parity Obligations, Subordinated Debt,

Special Facilities Debt, and any other obligations pertaining to the Airport System and (iii) except as otherwise provided in the next three paragraphs.

(A) The City may sell, exchange, lease, or otherwise dispose of, or exclude from the Airport System any property constituting a part of the Airport System which the Aviation Director certifies (i) to be no longer useful in the construction or operation of the Airport System, or (ii) to be no longer necessary for the efficient operation of the Airport System, or (iii) to have been replaced by other property of at least equal value. The net proceeds of the sale or disposition of any Airport System property (or the fair market value of any property so excluded) pursuant to this paragraph shall be used for the purpose of replacing properties at the Airport System, shall be paid into the Revenue Fund, or shall be applied to retire or pay Annual Debt Service Requirements of Parity Obligations.

(B) The preceding provisions to the contrary notwithstanding, the City will not enter into any lease of, or sell or otherwise dispose of, any part of the Airport System or enter into a management or other similar operating agreement for the operation of any part of the Airport System if, as a result of such lease, sale or other disposition, the interest income on any of the Parity Obligations would become includable in gross income of the recipients thereof for federal income tax purposes. Without limiting the generality of the foregoing, the City (i) will not take any action that would cause any part of the Airport System financed with the proceeds of Tax-Exempt Debt to cease to be "owned by" the City (as the term "owned by" is used in section 142(b)(1)(A) of the Code), (ii) will require, as a condition to the leasing of any part of the Airport System, or the entering into of any management or other similar operating agreement for the operation of any part of the Airport System, that the lessee or the other party to such management or other similar operating agreement, as the case may be, make an irrevocable election, in accordance with the provisions of section 142(b)(1)(B) of the Code and the regulations issued thereunder, not to claim depreciation or an investment credit with respect to the property leased to it by the City, or in the case of a management or other similar operating agreement, the property managed or operated by it, (iii) will not enter into any lease, management or other similar operating agreement with respect to any portion of the Airport System if such lease, management or other operating agreement has a term of eighty percent (80%) or more of the reasonably expected economic life of the property subject to such lease, management or other similar operating agreement within the meaning of section 142(b)(1)(B)(ii) of the Code, and (iv) will not enter into any lease, management or other similar operating agreement if the lessee or other party to a management or other similar operating agreement has an option to purchase any portion of the Airport System for a price other than the fair market value of such property at the time such option is exercised. The foregoing notwithstanding, the City shall not be obliged to comply with the aforesaid requirements of the Code during the term of Tax-Exempt Debt if the failure to comply with such requirements would not adversely affect the tax-exempt status of such Debt.

(C) Nothing herein prevents any transfer of all or a substantial part of the Airport System to another body corporate and politic (including, but not necessarily limited to, a joint action agency or an airport authority) which assumes the City's obligations under this Master Ordinance and in any Supplement, in whole or in part, if (i) in the written opinion of an Airport Consultant, the ability to meet the rate covenant under this Master Ordinance and in any Supplement are not materially and adversely affected and (ii) in the written opinion of Bond Counsel, such transfer and assumption will not cause the interest on any Outstanding Parity Obligations that are Tax-Exempt Debt to be includable in gross income of the owners thereof for federal income tax purposes. In such event, following such transfer and assumption, all references to the City, any City officials, City ordinances, City budgetary procedures and any other officials, actions, powers or characteristics of the City shall be deemed references to the transferee entity and comparable officials, actions, powers or characteristics of such entity. In the event of any such transfer and assumption, nothing therein shall prevent the retention by the City of any facility of the Airport System if, in the written opinion of an Underwriter, such retention will not materially and adversely affect nor unreasonably restrict the transferee entity's ability to comply with the requirements of the rate covenant and the other covenants of this Master Ordinance and any Supplement.

(h) **Special Facilities.** The City may finance Special Facilities from the proceeds of Special Facilities Debt issued by or on behalf of the City without regard to any requirements of this Master Ordinance with respect to the issuance of Parity Obligations, subject, however, to the following conditions:

(i) Such Special Facilities Debt shall be payable solely from rentals derived by or on behalf of the City under a Special Facilities Lease entered into between the City (or an entity acting on behalf of the City) and the person, firm or corporation which will be utilizing the Special Facilities to be financed; and

(ii) In addition to all rentals with respect to the Special Facilities to be financed, a fair and reasonable rental for the land upon which said Special Facilities are to be constructed shall be charged by the City, and said ground rent shall be deemed Gross Revenues not available for the payment of such Special Facilities Debt.

(i) **Accounts and Fiscal Year.** It shall keep proper books, records and accounts relating to the Airport System separate and apart from all other records and accounts of the City, in which complete and correct entries shall be made of all transactions relating to the Airport System, and the City shall cause said books and accounts to be audited annually as of the close of each Fiscal Year by an Accountant (which may be part of the City's comprehensive annual financial report). The City agrees to operate the Airport System and keep its books of records and account pertaining thereto on the basis of its current Fiscal Year.

(j) **Audits.** After the close of each Fiscal Year while any Parity Obligation is Outstanding, an audit will be made by an Accountant of the books and accounts relating to the Airport System and the Gross Revenues (which may be included in the City's comprehensive annual financial report). As soon as practicable after the close of each such Fiscal Year, and when said audit has been completed and made available to the City, a copy of such audit for the preceding Fiscal Year shall be mailed to the Municipal Advisory Council of Texas, any Bond Insurer or Credit Provider, and to any owner of any then Outstanding Parity Obligations who shall so request in writing promptly after it is readily available to the general public, and also to each information depository then required pursuant to Rule 15c2-12 promulgated by the Securities and Exchange Commission, or similar rule, within the time period required by such Rule 15c2-12. Such annual audit reports shall be open to the inspection of the owners of the Parity Obligations and their agents and representatives at all reasonable times during regular business hours of the City.

(k) **Annual Budget; Tax Levy for Operation and Maintenance; Elimination of Tax Levy.** The City shall prepare, prior to the beginning of each Fiscal Year, an Annual Budget for the Airport System (which may be included in the City's general annual budget), in accordance with law, reflecting an estimate of cash receipts and disbursements for the ensuing Fiscal Year in sufficient detail to indicate the probable Gross Revenues and Operation and Maintenance Expenses for such Fiscal Year. Such budget is required to contain, among other items, the following: estimated Gross Revenues, Operation and Maintenance Expenses and Net Revenues for such Fiscal Year, the estimated amounts to be deposited during such Fiscal Year in each of the Funds and Accounts established in this Master Ordinance and any Supplement, and the estimated expenditures during such Fiscal Year for the replacement of Capital Improvements. A copy of the Annual Budget shall be filed with any Bond Insurer or Credit Provider promptly after it is readily available to the general public.

(l) **Insurance.** The City shall cause to be insured such parts of the Airport System as would usually be insured by corporations operating like properties, with a responsible insurance company or companies, against risks, accidents or casualties against which and to the extent insurance is usually carried by corporations operating like properties, including, to the extent reasonably obtainable, fire and extended coverage insurance and public liability and property damage insurance; provided, however, that public liability and property damage insurance need not be carried if the City Attorney gives a written opinion to the effect that the City is not liable for claims which would be protected by such insurance. All insurance premiums shall be paid as an expense of operation of the Airport System. At any time while any contractor engaged in construction work shall be fully responsible therefor, the City shall not be required to carry insurance on the work being constructed if the contractor is required to carry appropriate insurance. All such policies shall be open to the inspection of the Bondholders and their representatives at all reasonable times. Upon the happening of any loss or damage covered by insurance from one or more of said causes, the City shall make due proof of loss and shall do all things necessary or desirable to cause the insuring companies to make payment in full directly to the City. The proceeds of insurance covering such property, together with any other funds necessary and available for such purpose, shall be used forthwith by the City for repairing the property damaged or replacing the property destroyed; provided, however, that if said insurance proceeds and other funds are insufficient for such purpose, then said insurance proceeds pertaining to the Airport System shall be deposited in a special and separate trust fund, at the Depository, to be designated the "Insurance Account". The Insurance Account shall be held until such time as other funds become available which, together with the Insurance Account, will be sufficient to make the repairs or replacements originally required.

(m) **Governmental Agencies.** The City will duly observe and comply with all valid requirements of all Federal and State authorities relative to the ownership, operation, and maintenance of the Airport System. Additionally, the City will comply with all of the terms and conditions of any and all grants and assurances, franchises, permits and authorizations applicable to or necessary with respect to the Airport System, and which have been obtained from any governmental agency; and the City has or will obtain and keep in full force and effect all franchises, permits, authorization and other requirements applicable to or necessary with respect to the acquisition, construction, equipment, operation and maintenance of the Airport System.

(n) **Rights of Inspection.** The owner of Parity Obligations shall have the right at all reasonable times during regular business hours of the City to inspect all records, accounts and data of the City relating to the Airport System.

(o) **Legal Holidays.** In any case where the date of maturity of interest on or principal of the Parity Obligations or the date fixed for redemption of any Parity Obligations or any other payment obligation under a Parity Obligation not be a Business Day, then payment of interest or principal need not be made on such date but may be made on the next succeeding Business Day with the same force and effect as if made on the date of maturity or the date fixed for redemption and no interest shall accrue for the period from the date of maturity or redemption to the date of actual payment.

(p) **Bondholders' Remedies.** This Master Ordinance and any Supplement shall constitute a contract between the City and the owners of the Parity Obligations from time to time Outstanding and this Master Ordinance and the Supplement authorizing the issuance of Parity Obligations shall be and remain irrevocable until the Parity Obligations and any interest thereon shall be fully paid or discharged or provision therefor shall have been made as provided in a Supplement. In the event of a default in the payment of the principal of or interest on any Parity Obligation or a default in the performance of any duty or covenant provided by law or in this Master Ordinance, the owner or owners of any Parity Obligation may pursue all legal remedies afforded by the Constitution and laws of the State of Texas to compel the City to remedy such default and to prevent further default or defaults. Without in any way limiting the generality of the foregoing, it is expressly provided that any owner of any Parity Obligation may at law or in equity, by suit, action, mandamus, or other proceedings filed in any court of competent jurisdiction, enforce and compel performance of all duties required to be performed by the City under this Master Ordinance and any Supplement, including the making of reasonably required rates and charges for the use and services of the Airport System, the deposit of the Gross Revenues into the Funds and Accounts provided in this Master Ordinance and any Supplement, and the application of such Gross Revenues in the manner required in this Master Ordinance and any Supplement.

SECTION 5. CREATION OF FUNDS AND ACCOUNTS. The following special Funds and Accounts have been created and established in connection with the issuance of the Pre-2001 Parity Obligations and shall continue to be maintained on the books of the City, so long as any of the Parity Obligations, or interest thereon, are Outstanding and unpaid:

(a) *City of San Antonio Airport System Revenue Fund*, herein called the "Revenue Fund"; and there has been created and there shall continue to be maintained within the Revenue Fund an account entitled the San Antonio Airport System Operation and Maintenance Account, herein called the "Operation and Maintenance Account";

(b) *City of San Antonio Airport System Parity Obligations Bond Fund*, herein called the "Bond Fund";

(c) *City of San Antonio Airport System Parity Obligations Reserve Fund*, herein called the "Bond Reserve Fund";

(d) *City of San Antonio Airport System Parity Obligations Special Contingency Reserve Fund*, herein called the "Special Contingency Reserve Fund"; and

(e) *City of San Antonio Airport System Capital Improvement Fund*, herein called the "Capital Improvement Fund".

SECTION 6. REVENUE FUND. All Gross Revenues shall be kept and accounted for separate and apart from all other funds of the City and shall be credited from day to day as received to the credit of the Revenue Fund. Gross Revenues in the Revenue Fund shall be deposited to the credit of the other Funds and Accounts created or maintained by this Master Ordinance, in the manner and amounts hereinafter provided, and each of such Funds and Accounts shall have priority as to such deposits in the order in which they are treated in the following Sections 7 through 12.

SECTION 7. BOND FUND. (a) *Purpose of and Payments into the Bond Fund.* The Bond Fund shall be used solely to pay the principal of, premium, if any, and interest on, and other payments (other than Operation and Maintenance Expenses) incurred in connection with Parity Obligations, as such principal matures and such interest and other payments comes due. There shall be credited to the Bond Fund the following:

(1) immediately after the sale and delivery of any series of Parity Obligations, any accrued interest on such Parity Obligations; and

(2) on or before the 25th day of each month, commencing with the month following the delivery of each series of Parity Obligations, such amounts, in approximately equal monthly installments, as will be sufficient, together with any other funds on deposit therein and available for such purpose, to pay the principal of, premium, if any and interest on, and other payments scheduled to come due on all Outstanding Parity Obligations on the next applicable payment date.

(b) *Accounts.* The City reserves the right in any Supplement to (i) establish within the Bond Fund various Accounts to facilitate the timely payment of Parity Obligations as the same become due and owing and (ii) provide other terms and conditions with respect to payment obligations with respect to a Parity Obligation not inconsistent with the provisions of this Master Ordinance.

SECTION 8. BOND RESERVE FUND. (a) *Payments into the Bond Reserve Fund.* There is currently on deposit in the Bond Reserve Fund an amount at least equal to the Average Annual Debt Service Requirements of the Pre-2001 Parity Obligations. After the delivery of any future Additional Parity Obligations, the City shall cause the Bond Reserve Fund to be increased, if and to the extent necessary, so that such fund will contain an amount of money and investments equal in market value to the Average Annual Debt Service Requirements of all Parity Obligations which will be Outstanding after such delivery. An amount of money and investments equal in market value to the Average Annual Debt Service Requirements of all Parity Obligations at any time Outstanding is hereby designated as the "Required Reserve Amount". Any increase in the Required Reserve Amount may be funded from Gross Revenues, or from proceeds from the sale of any Additional Parity Obligations, or any other available source or combination of sources. All or any part of the Required Reserve Amount not funded initially and immediately after the delivery of any installment or issue of Additional Parity Obligations shall be funded, within not more than five years from the date of such delivery, by deposits of Gross Revenues in approximately equal monthly installments on or before the 25th day of each month. Principal amounts of Parity Obligations which must be redeemed pursuant to any applicable mandatory redemption requirements shall be deemed to be maturing amounts of principal for the purpose of calculating principal and interest requirements on such bonds. When and so long as the amount in the Bond Reserve Fund is not less than the Required Reserve Amount no deposits shall be made to the credit of the Bond Reserve Fund; but when and if the Bond Reserve Fund at any time contains less than the Required Reserve Amount, then the City shall transfer from Gross Revenues in the Revenue Fund, and deposit to the credit of the Bond Reserve Fund, monthly, on or before the 25th day of each month, a sum equal to 1/60th of the Required Reserve Amount, until the Bond Reserve Fund is restored to the Required Reserve Amount. The City specifically covenants that when and so long as the Bond Reserve Fund contains the Required Reserve Amount, the City shall cause all interest and income derived from the deposit or investment of the Bond Reserve Fund to be deposited to the credit of the Bond Fund.

(b) *Purpose.* The Bond Reserve Fund shall be used to pay the principal of or interest on all Parity Obligations at any time when the Bond Fund is insufficient for such purpose, and may be used finally to retire the last debt service requirements on the Parity Obligations.

(c) *Authority to Use Credit Facility.* The City may satisfy its covenant to maintain the Bond Reserve Fund in an amount equal to the Required Reserve Amount with a Credit Facility that will provide funds, together with other Reserve Fund Obligations, if any, credited to the Bond Reserve Fund, at least equal to the Required Reserve Amount. The City may replace or substitute a Credit Facility for all or a portion of the cash or Eligible Investments on deposit in the Bond Reserve Fund or in substitution for or replacement of any existing Credit Facility. Upon such replacement or substitution, cash or Eligible Investments on deposit in the Bond Reserve Fund which, taken together with the face amount of any existing Credit Facilities, are in excess of the Required Reserve Amount may be withdrawn by the City, at the option of the Designated Financial Officer, and transferred to the Bond Fund (or to the Revenue Fund if the City receives an opinion of Bond Counsel that transferring such funds to the Revenue Fund would not adversely effect the tax exempt status of any Outstanding Parity Obligations originally issued as Tax-Exempt Debt; provided that withdrawn cash constituting bond proceeds shall be used only for Airport System Improvements); provided, however, that at the option of the Designated Financial Officer, acting on behalf of the City, the face amount of any Credit Facility for the Bond Reserve Fund may be reduced in lieu of such transfer.

(d) ***Withdrawals from Bond Reserve Fund.*** If the City is required to make a withdrawal from the Bond Reserve Fund for any of the purposes described in this Section, the Designated Financial Officer, acting on behalf of the City, shall promptly notify the issuer of such Credit Facility of the necessity for a withdrawal from the Bond Reserve Fund for any such purposes, and shall make such withdrawal FIRST from available moneys or Eligible Investments then on deposit in the Bond Reserve Fund, and NEXT from a drawing under any Credit Facility to the extent of such deficiency. Should there be more than one provider of Credit Facilities that are on deposit in or credited to the Bond Reserve Fund, the order of priority with respect to the drawings on such Credit Facilities shall be determined by the City and the providers of the Credit Facilities prior to any such drawings being made thereunder.

(e) ***Deficiencies.*** In the event of a deficiency in the Bond Reserve Fund, such that the Bond Reserve Fund contains less than the Required Reserve Amount, then the City shall restore the Required Reserve Amount in the manner described in Section 8(a) above. In the event the Required Reserve Amount is funded through the use of a Credit Facility, and the Credit Facility specifies a termination or expiration date that is prior to the final maturity of the Parity Obligations so secured thereby, the City shall provide that such Credit Facility shall be renewed at least twelve (12) months prior to the specified termination or expiration date or in the alternative provide that any deficiency that will result upon the termination or expiration of such Credit Facility will be accounted for either by (i) obtaining a substitute Credit Facility no sooner than twenty-four (24) months or no later than twelve (12) months prior to the specified termination or expiration date of the then existing Credit Facility or (ii) by depositing cash into the Bond Reserve Fund in no more than twenty-four (24) monthly installments of not less than one-twenty fourth (1/24th) of the amount of such deficiency on or before the 25th day of each month, commencing on the 25th day of the month which is twelve (12) months prior to such termination or expiration date, to restore the Bond Reserve Fund to the Required Reserve Amount.

(f) ***Redemption or Defeasance.*** In the event of the redemption or defeasance of any Parity Obligation, any Reserve Fund Obligations on deposit in the Bond Reserve Fund in excess of the Required Reserve Amount may be withdrawn and transferred, at the option of the City, to the Bond Fund, as a result of (i) the redemption of the Parity Obligations, or (ii) funds for the payment of the Parity Obligations having been deposited irrevocably with the paying agent or place of payment therefor in the manner described in a Supplement, the result of such deposit being that such Parity Obligations no longer are deemed to be Outstanding under the terms of this Master Ordinance and such Supplement.

(g) ***Credit Facility Draws.*** In the event there is a draw upon the Credit Facility, the City shall reimburse the issuer of such Credit Facility for such draw, in accordance with the terms of any agreement pursuant to which the Credit Facility is issued, from Gross Revenues; however, such reimbursement from Gross Revenues shall be subject to the provisions of Section 7(d) hereof and shall be subordinate and junior in right of payment to the payment of principal of and premium, if any, and interest on Parity Obligations.

SECTION 9. OPERATION AND MAINTENANCE ACCOUNT IN THE REVENUE FUND; PAYMENT OF OPERATION AND MAINTENANCE EXPENSES AND TRANSFERS TO SUBORDINATED DEBT FUND.

All amounts in the Revenue Fund in excess of those required to be made to the credit of the Bond Fund and the Bond Reserve Fund shall be deemed to constitute, and shall be designated as, the Operation and Maintenance Account in the Revenue Fund. The amounts in the Operation and the Maintenance Account shall be, first, used to pay all Operation and Maintenance Expenses, and second, transferred to the Subordinated Debt Fund (authorized to be established in a Supplement pursuant to Section 10 of this Master Ordinance) at the times and in the amounts required by a Supplement to provide for the payment of principal, premium, if any, and interest on, and other payments (excluding any Operation and Maintenance Expenses but including payments to a related debt service reserve fund) incurred in connection with, any Subordinated Debt. Such payments and transfers described in the preceding sentence shall have priority over all deposits to the credit of the Special Contingency Reserve Fund and the Capital Improvement Fund as hereinafter provided. It is further specifically provided that no deposit shall ever be made to the credit of the Special Contingency Reserve Fund or the Capital Improvement Fund if any such deposit would reduce the amount on hand in the Operation and Maintenance Account to less than the budgeted or estimated Operation and Maintenance Expenses for the ensuing three calendar months.

SECTION 10. SUBORDINATED DEBT FUND. (a) ***Subordinated Debt Fund Authorized to be Established.*** For the sole purpose of paying the principal amount of, premium, if any, and interest on, and other payments (excluding any Operation and Maintenance Expenses but including payments to a related debt service reserve fund) incurred in connection with Subordinated Debt, the City may create in a Supplement which authorizes the issuance of Subordinated Debt a separate fund designated as the Subordinated Debt Fund. Such Subordinated Debt Fund shall be established and maintained on the books of the City and accounted for separate and apart from all other funds of the City. Moneys in the Subordinated Debt Fund shall be deposited and maintained in an official depository bank of the City.

(b) **Additional Accounts.** The City may create, establish and maintain on the books of the City additional Accounts within the Subordinated Debt Fund from which moneys can be withdrawn to pay the principal of and interest on Subordinated Debt which hereafter may be issued or incurred.

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SECTION 12. CAPITAL IMPROVEMENT FUND. Subject to satisfying the requirements of Sections 7, 8, 9, 10 and 11 of this Master Ordinance, the City shall transfer the balance remaining in the Operation and Maintenance Account in the Revenue Fund at the end of each Fiscal Year and deposit same to the credit of the Capital Improvement Fund. The Capital Improvement Fund shall be used for the purposes, and with priority of claim thereon, as follows: first, for the payment of principal, interest, and reserve requirements on Parity Obligations if funds on deposit in the Bond Fund and the Bond Reserve Fund are insufficient to make such payments; second, for the payment of principal, interest, and reserve requirements on Subordinated Debt if funds on deposit in the Subordinated Debt Fund and any related debt service reserve fund are insufficient to make such payments; third, for the purpose of paying the costs of improvements, enlargements, extensions, additions, replacements, repairs or other capital expenditures related to the Airport System; and fourth, for any other lawful purpose related to the Airport System.

SECTION 13. CONSTRUCTION FUND AND REBATE FUND. The City, in a Supplement, hereafter may create, establish and maintain on the books of the City a separate Fund or Account for use by the City for payment of all lawful costs associated with the construction, improvement and equipping of the Airport System, and for making payments to the United States of America pursuant to section 148 of the Code.

SECTION 14. DEFICIENCIES IN FUNDS. If in any month the City shall fail to deposit into the Bond Fund or Bond Reserve Fund the amounts required, amounts equivalent to such deficiencies shall be set apart and paid into said Funds from the first available and unallocated Gross Revenues for the following month or months, and such payments shall be in addition to the amounts otherwise required to be paid into said Funds during such month or months. To the extent necessary, the City shall increase the rates, fees, charges, and amounts for the use, occupancy, services, facilities and operation of the Airport System to make up for any such deficiencies.

SECTION 15. SECURITY FOR FUNDS. All Funds and Accounts created or maintained by this Master Ordinance shall be secured in the manner and to the fullest extent permitted or required by law for the security of public funds, and such Funds and Accounts shall be used only for the purposes and in the manner permitted or required by this Master Ordinance.

SECTION 16. PAYMENT OF PARITY OBLIGATIONS. On or before each principal and interest payment date while any of the Parity Obligations are Outstanding and unpaid, the City shall make available to the paying agents therefor, out of the Bond Fund, or if necessary, out of the Bond Reserve Fund, money sufficient to pay, on each of such dates, the principal of and interest on the Parity Obligations as the same matures and comes due, or to redeem the Parity Obligations prior to maturity, either upon mandatory redemption or at the option of the City. The Paying Agents shall destroy all paid Parity Obligations, and the coupons appertaining thereto, if any, and furnish the City with an appropriate certificate of cancellation or destruction if requested by the City.

SECTION 17. ISSUANCE OF ADDITIONAL PARITY OBLIGATIONS. (a) **Additional Parity Obligations.** The City reserves the right to issue or incur, for any lawful purpose, pursuant to this Master Ordinance and a Supplement, Additional Parity Obligations; provided, however, that no such Parity Obligations shall be delivered unless:

- (i) No Default. The Designated Financial Officer and the Aviation Director certify that, upon incurring, issuing or otherwise becoming liable in respect to such Parity Obligations, the City will not be in default under any term or provision of this Master Ordinance, any Parity Obligations then Outstanding or any Supplement pursuant to which any of such Parity Obligations were issued or incurred.
- (ii) Proper Fund Balances. The Designated Financial Officer certifies that, upon the issuance of such Parity Obligations, the Bond Fund will have the required amounts on deposit therein and that the Bond Reserve Fund will contain the applicable Required Reserve Amount or so much thereof as is required to be funded at such time. Upon the issuance of such Parity Obligations, any additional amounts necessary to cause the Bond Reserve Fund to be funded in the Required Reserve Amount may be funded over a 60-month period in the manner provided for in Section 8(a) of this Master Ordinance, with a Credit Facility in the manner provided in Section 8(c) of this Master Ordinance, or a combination thereof.

(iii) **Projected Coverage.** An Airport Consultant provides a written report setting forth projections which indicate that the estimated Net Revenues of the Airport System for each of three consecutive Fiscal Years beginning in the later of:

- (A) the first complete Fiscal Year following the estimated date of completion and initial use of all revenue producing facilities to be financed with Parity Obligations, based upon a certified written estimated completion date by the consulting engineer for such facility or facilities, or
- (B) the first complete Fiscal Year in which the City will have scheduled payments of interest on or principal of the Parity Obligations to be issued for the payment of which provision has not been made as indicated in the report of such Airport Consultant from proceeds of such Parity Obligations, investment income thereon or from other appropriated sources (other than Net Revenues),

are equal to at least 1.25 times of the Annual Debt Service Requirements on all Parity Obligations scheduled to occur during each such respective Fiscal Year after taking into consideration the additional Annual Debt Service Requirements for the Additional Parity Obligations then being issued or incurred.

(iv) **Alternative Coverage for Parity Obligations.** In lieu of the certification in clause (iii) above, the Designated Financial Officer may provide a certificate showing that, for either the City's most recent complete Fiscal Year or for any consecutive 12 out of the most recent 18 months, the Net Revenues of the Airport System were equal to at least 1.25 times of the maximum Annual Debt Service Requirements on all Parity Obligations scheduled to occur in the then current or any future Fiscal Year after taking into consideration the Parity Obligations proposed to be issued or incurred.

(b) **Refunding Obligations.** If Parity Obligations are being issued for the purpose of refunding less than all Outstanding Parity Obligations, neither of the certifications described in subsections (a)(iii) or (a)(iv) of this Section are required so long as the Designated Financial Officer provides a certificate showing that the aggregate debt service requirements of such refunding Parity Obligations will not exceed the aggregate debt service requirements of the Parity Obligations being refunded.

(c) **Completion Obligations.** The City reserves the right to issue or incur Parity Obligations to pay the cost of completing any Capital Improvements for which Parity Obligations have previously been issued.

Prior to the delivery of Completion Obligations, the City must provide, in addition to all of the applicable certificates required by subsection (a) of this Section (other than the certificates not required under the circumstances described below), the following documents:

- (i) a certificate of the consulting engineer engaged by the City to design the Capital Improvement for which the Completion Obligations are to be delivered stating that such Capital Improvement has not materially changed in scope since the most recent series of Parity Obligations was issued or incurred for such purpose (except as permitted in the Supplement authorizing such Parity Obligations) and setting forth the aggregate cost of the Capital Improvement which, in the opinion of such consulting engineer, has been or will be incurred; and
- (ii) a certificate of the Aviation Director (A) stating that all amounts allocated to pay costs of the Capital Improvement from the proceeds of the most recent series of Parity Obligations issued or incurred in connection with the Capital Improvement for which the Completion Obligations are being issued or incurred were used or are still available to be used to pay costs of such Capital Improvement; (B) containing a calculation of the amount by which the aggregate cost of that Capital Improvement (furnished in the consulting engineer's certificate described above) exceeds the sum of the costs of the Capital Improvement paid to such date plus the moneys available at such date within any construction fund or other like account applicable to the Capital Improvement plus any other moneys which the Aviation Director, in the discretion thereof, has determined are available to pay such costs in any other fund; and (C) certifying that, in the opinion of the Aviation Director, it is necessary to issue or

incur the Completion Obligations to provide funds for the completion of the Capital Improvement.

Completion Obligations may be issued or incurred for any Airport System facility or project which shall be declared in the Supplement to be a Capital Improvement. Any such Supplement may contain such further provisions as the City shall deem appropriate with regard to the use, completion, modification or abandonment of such Capital Improvement. Anything herein to the contrary, the provisions of subsections (a)(iii) and (a)(iv) of this Section do not apply to Completion Obligations if the aggregate principal amount of the Completion Obligations then to be issued does not exceed 15% of the aggregate principal amount of the Parity Obligations initially issued to pay the cost of such Capital Improvement.

(d) ***Subordinated Debt and Special Facilities Debt.*** Subordinated Debt and Special Facilities Debt may be issued or incurred by the City without limitation. Subordinated Debt shall be payable from moneys deposited to the credit of the Subordinated Debt Fund. Special Facilities Debt is permitted to be issued, as described in Section 4(g) hereof, and shall not be secured by a lien on and pledge of Gross Revenues or Net Revenues.

(e) ***Credit Agreements.*** Payments to be made under a Credit Agreement may be treated as Parity Obligations if the governing body of the City makes a finding in the Supplement authorizing the treatment of the obligations of the City incurred under a Credit Agreement as a Parity Obligation that, based upon the findings contained in a certificate executed and delivered by a Designated Financial Officer, the City will have sufficient funds to meet the financial obligations of the Airport System, including sufficient Net Revenues to satisfy the Annual Debt Service Requirements of the Airport System and the financial obligations of the City relating to the Airport System after giving effect to the treatment of the Credit Agreement as a Parity Obligation.

(f) ***Determination of Net Revenues.*** In making a determination of Net Revenues for any of the purposes described in this Section, the Airport Consultant or the Designated Financial Officer may take into consideration a change in the rates and charges for services and facilities afforded by the Airport System that became effective at least 30 days prior to the last day of the period for which Net Revenues are determined and, for purposes of satisfying the Net Revenues tests described above, make a pro forma determination of the Net Revenues of the Airport System for the period of time covered by the certification or opinion based on such change in rates and charges being in effect for the entire period covered by the certificate or opinion.

SECTION 18. DEFEASANCE. The provisions relating to the terms and conditions upon which a defeasance of Parity Obligations shall be effected shall be contained in the Supplement authorizing such Parity Obligations.

SECTION 19. AMENDMENT OF MASTER ORDINANCE. The City hereby reserves the right to amend this Master Ordinance subject to the following terms and conditions, to-wit:

(a) ***Amendments Without Consent of Holders or Credit Providers.*** The City may from time to time, with notice to each Credit Provider but without the consent of any Holder, except as otherwise required by paragraph (b) below, amend this Master Ordinance in order to:

- (1) cure any ambiguity, defect or omission in this Master Ordinance that does not materially adversely affect the interests of the Holders;
- (2) grant additional rights or security for the benefit of the Holders;
- (3) add events of default as shall not be inconsistent with the provisions of this Master Ordinance and which shall not materially adversely affect the interests of the Holders;
- (4) qualify this Master Ordinance under the Trust Indenture Act of 1939, as amended, or corresponding provisions of federal laws from time to time in effect;
- (5) make such amendments to this Master Ordinance as may be required, in the opinion of Bond Counsel, to ensure compliance with sections 103 and 141 through 150 of the Code and the regulations promulgated thereunder and applicable thereto;

(6) make such changes, modifications or amendments as may be necessary or desirable in order to allow the owners of the Parity Obligations to thereafter avail themselves of a book-entry system for payments, transfers and other matters relating to the Parity Obligations, which changes, modifications or amendments are not contrary to or inconsistent with other provisions of this Master Ordinance and which shall not adversely affect the interests of the owners of the Parity Obligations;

(7) make such changes, modifications or amendments as may be necessary or desirable in order to obtain the approval of the Parity Obligations by the Office of the Attorney General of the State of Texas, to the extent such approval is required by law, or to obtain or maintain the granting of a rating on the Parity Obligations by a Credit Rating Agency, or to obtain or maintain a Credit Agreement or a Credit Facility;

(8) make such changes, modifications or amendments as may be necessary or desirable, which shall not adversely affect the interests of the owners of the Parity Obligations, in order, to the extent permitted by law, to facilitate the economic and practical utilization of interest rate swap agreements, foreign currency exchange agreements, or similar types of agreements with respect to the Parity Obligations; and

(9) make any other change (other than any change described in clauses (1) through (5) of subsection (b) below) with respect to which the City receives written confirmation from each Rating Agency that such amendment would not cause such Rating Agency to withdraw or reduce its then current rating on the Parity Obligations.

Notice of any such amendment of the nature described in this Section 19(a) may be provided in the manner described in Section 19(c) hereof; provided, however, that the giving of such notice shall not constitute a condition precedent to the adoption of an ordinance providing for such amendment, and the failure to provide such notice shall not adversely affect the implementation of such amendment as adopted pursuant to such amendatory ordinance.

(b) ***Amendments With Consent of Holders and Credit Providers.*** Except as provided in Section 19(a) above, each Credit Provider and the Holders of Parity Obligations aggregating a majority in principal amount of the aggregate principal amount of then Outstanding Parity Obligations which are the subject of a proposed amendment or are affected by a proposed amendment shall have the right from time to time to approve any amendment to this Master Ordinance which may be deemed necessary or desirable by the City; provided, however, that without the consent of 100% of the Holders in aggregate principal amount of the then Outstanding Parity Obligations affected by such amendment, nothing herein contained shall permit or be construed to permit amendment of the terms and conditions of this Master Ordinance or in any of the Parity Obligations affected by such amendment so as to:

- (1) Make any change in the maturity of any of such Parity Obligations;
- (2) Reduce the rate of interest borne by any of such Parity Obligations;
- (3) Reduce the amount of the principal of, or redemption premium, if any, payable on any of such Parity Obligations;
- (4) Modify the terms of payment of principal or of interest or redemption premium on such Outstanding Parity Obligations or any of them or impose any condition with respect to such payment; or
- (5) Change the minimum percentage of the principal amount of the Parity Obligations necessary for consent to such amendment.

(c) ***Notice of Amendment.*** Whenever the City shall desire to make any amendment or addition to or rescission of this Master Ordinance requiring consent of each Credit Provider and/or the Holders of the Parity Obligations, the City shall cause notice of the amendment, addition, or rescission to be sent by first class mail, postage prepaid, to (i) each Credit Provider, and (ii) the Holders (if the Holders of all Parity Obligations or at least a majority in aggregate principal amount of the Parity Obligations are required to consent) at the respective addresses shown on the Registration Books. Whenever at any time within one year after the date of the giving of such notice, the City shall receive an instrument or instruments in writing executed by each Credit Provider and the Holders of all or a majority (as the case may be) in aggregate principal amount of the Parity Obligations then outstanding affected by any such amendment, addition, or rescission requiring the consent of the Holders, which instrument or instruments shall refer to the proposed amendment, addition, or rescission described in such notice and shall specifically consent to and approve the adoption thereof in

substantially the form of the copy thereof referred to in such notice, thereupon, but not otherwise, the City may adopt such amendment, addition, or rescission in substantially such form, except as herein provided.

(d) ***Amendments Binding on All Holders.*** No Holder may thereafter object to the adoption of any amendment, addition, or rescission which is accomplished pursuant to and in accordance with the provisions of this Section, or to any of the provisions thereof, and such amendment, addition, or rescission shall be fully effective for all purposes.

(e) ***Consents Irrevocable and Binding on Future Holders.*** Any consent given by the Holder of a Parity Obligation pursuant to the provisions of this Section shall be irrevocable for a period of six months from the date of the publication of the notice provided for in this Section, and shall be conclusive and binding upon all future Holders of the same Parity Obligation during such period. Such consent may be revoked at any time after six months from the date of the publication of said notice by the Holder who gave such consent, or by a successor in title, by filing notice with the City, but such revocation shall not be effective if the Holders of a majority in aggregate principal amount of the affected Parity Obligations then Outstanding, have, prior to the attempted revocation, consented to and approved the amendment.

(f) ***Ownership of Parity Obligations.*** For the purposes of establishing ownership of the Parity Obligations, the City shall rely solely upon the registration of the ownership of such Parity Obligations on the registration books kept by the Paying Agent/Registrar.

(g) ***Ownership.*** For the purpose of this Section, the ownership and other matters relating to all Parity Obligations shall be determined as provided in each Supplement.

(h) ***Amendments of Supplements.*** Each Supplement shall contain provisions governing the ability of the City to amend such Supplement; provided, however, that no amendment may be made to any Supplement for the purpose of granting to the owners of Outstanding Parity Obligations under such Supplement a priority over the owners of any other Outstanding Parity Obligations.

SECTION 20. INVESTMENTS. Money in any Fund established pursuant to this Master Ordinance or any Supplement may, at the option of the City, be invested in any investment permitted by the provisions of the Public Funds Investment Act (Chapter 2256, Texas Government Code, as amended); provided that all such deposits and investments shall be made in such manner that the money required to be expended from any Fund will be available at the proper time or times. Such investments shall be valued in terms of current market value as of the last day of each Fiscal Year of the City. All interest and income derived from such deposits and investments immediately shall be credited to, and any losses debited to, the Fund from which the deposit or investment was made, except to the extent otherwise provided in Section 8 and 11 of this Master Ordinance with respect to the Bond Reserve Fund and Special Contingency Reserve Fund. Such investments shall be sold promptly when needed or when necessary to prevent any default in connection with the Parity Obligations, consistent with the ordinances, respectively, authorizing their issuance. It is further provided, however, that any interest earnings on proceeds of Parity Obligations, or on funds on deposit in any Fund or Account, which are required to be rebated to the United States of America in order to prevent any Parity Obligations from being arbitrage bonds shall be deposited to the Rebate Fund authorized to be established by a Supplement in accordance with Section 13 of this Master Ordinance and shall not be considered as interest earnings for the purposes of this Section or for the purposes of determining Gross Revenues.

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**THE FOLLOWING SECTIONS 7, 8, 9, 11 AND 13 APPEAR IN THE
EIGHTH SUPPLEMENT TO THE MASTER ORDINANCE**

SECTION 7. SECURITY. (a) ***Gross Revenues.*** The Series 2006 Bonds are special obligations of the City payable from and secured solely by the Gross Revenues pursuant to the Master Ordinance and this Eighth Supplement. The Gross Revenues are hereby pledged to the payment of the principal of, premium, if any, and interest on the Series 2006 Bonds as the same shall become due and payable.

(b) ***Bond Reserve Fund.*** The Series 2006 Bonds are to be secured by the Bond Reserve Fund. The City certifies that the amount currently on deposit in the Bond Reserve Fund (composed of cash and one Credit Facility issued in connection with the Refunded Bonds) is at least equal to the Required Reserve Amount relating to the Outstanding Parity Obligations, and the Required Reserve Amount will not increase upon delivery of the Series 2006 Bonds due to the fact that, concurrent with delivery of the Series 2006 Bonds, the Refunded Bonds will be defeased and will no longer

be Outstanding, and the City will realize annual debt service savings with respect to the Parity Obligations. Consequently, the Average Annual Debt Service Requirements will not increase; however, due to the fact that the Credit Facility issued in connection with the Refunded Bonds will terminate upon the issuance of the Series 2006 Bonds and the defeasance of the Refunded Bonds, and in order to comply with the requirements of Section 8(a) of the Master Ordinance, the City will purchase a Credit Facility in the form of a reserve fund surety policy from Financial Security Assurance (the "Series 2006 Reserve Fund Credit Facility") having a maximum amount to be drawn thereon equal to \$600,000, which amount, together with cash and investments currently on deposit in the Bond Reserve Fund, will cause the amount on deposit in the Bond Reserve Fund upon the issuance of the Series 2006 Bonds to be at least equal to the Required Reserve Amount. The Series 2006 Reserve Fund Credit Facility will be credited to the Bond Reserve Fund upon the issuance of the Series 2006 Bonds. For so long as said the Series 2006 Reserve Fund Credit Facility is in effect, the ordinance requirements of Financial Security Assurance, as a condition to the issuance of the Series 2006 Reserve Fund Credit Facility, attached hereto as *Exhibit C* hereto, are incorporated by reference into this Eighth Supplement and made a part hereof for all purposes, notwithstanding any other provision of this Eighth Supplement to the contrary. If deemed necessary by the Attorney General's Public Finance Division in connection with their approval of the Series 2006 Bonds, the City Manager, any Assistant City Manager and any Assistant to the City Manager are hereby authorized to enter into an agreement with Financial Security Assurance to further evidence the requirements and the City's obligations set forth in *Exhibit C*.

(c) **Security Interest.** Chapter 1208, Texas Government Code, applies to the issuance of the Series 2006 Bonds and the pledge of Gross Revenues by the City under the Master Ordinance and this Eighth Supplement, and is therefore valid, effective, and perfected. If Texas law is amended at any time while the Series 2006 Bonds are outstanding and unpaid such that the pledge of the Gross Revenues by the City under the Master Ordinance and this Eighth Supplement is to be subject to the filing requirements of Chapter 9, Texas Business & Commerce Code, then in order to preserve to the registered owners of the Series 2006 Bonds the perfection of the security interest in said pledge, the City agrees to take such measures as it determines are reasonable and necessary under Texas law to comply with the applicable provisions of Chapter 9, Texas Business & Commerce Code, and enable a filing to perfect the security interest in said pledge to occur.

SECTION 8. PAYMENTS; BOND FUND. (a) ***Moneys Made Available to Paying Agent.*** The City agrees to pay the principal of, premium, if any, and the interest on the Series 2006 Bonds when due. The City shall make available to the Paying Agent/Registrar, on or before such principal or interest payment date, money sufficient to pay such interest on and such principal of the Series 2006 Bonds as will accrue or mature. The Paying Agent/Registrar shall cancel all paid Series 2006 Bonds and shall furnish the City with an appropriate certificate of cancellation.

(b) ***Bond Fund.*** Pursuant to Section 7 of the Master Ordinance, moneys in the Revenue Fund shall be applied by the City on the dates and in the amounts, and in the order of priority with respect to the Funds and Accounts that such applications are described in the Master Ordinance, including making monthly deposits into the Bond Fund to provide sufficient funds to pay all principal of and interest on all Parity Obligations, including the Series 2006 Bonds.

SECTION 9. REBATE FUND. There is hereby created and there shall be established and maintained on the books of the City, and accounted for separate and apart from all other funds of the City, a separate fund designated as the Rebate Fund. The Rebate Fund shall be for the sole benefit of the United States of America and shall not be subject to the lien created by this Eighth Supplement or to the claim of any other Person, including the Holders of the Series 2006 Bonds. Amounts deposited to the Rebate Fund, together with any investment earnings thereon, shall be held in trust and applied solely as provided in section 148 of the Code.

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SECTION 11. AMENDMENT OF SUPPLEMENT. (a) ***Amendments Without Consent.*** This Eighth Supplement and the rights and obligations of the City and of the owners of the Series 2006 Bonds may be modified or amended at any time without notice to or the consent of any owner of the Series 2006 Bonds or any other Parity Obligations (but with prior notice to the Insurer), solely for any one or more of the following purposes:

(i) To add to the covenants and agreements of the City contained in this Eighth Supplement, other covenants and agreements thereafter to be observed, or to surrender any right or power reserved to or conferred upon the City in this Eighth Supplement;

(ii) To cure any ambiguity or inconsistency, or to cure or correct any defective provisions contained in this Eighth Supplement, upon receipt by the City of an opinion of Bond Counsel, that the same is needed for such purpose, and will more clearly express the intent of this Eighth Supplement;

(iii) To supplement the security for the Series 2006 Bonds, replace or provide additional credit facilities, or change the form of the Series 2006 Bonds or make such other changes in the provisions hereof as the City may deem necessary or desirable and which shall not, in the judgment of the City, materially adversely affect the interests of the owners of the Outstanding Series 2006 Bonds;

(iv) To make any changes or amendments (A) requested by any Credit Rating Agency then rating or requested by the City to rate Parity Obligations, as a condition to the issuance or maintenance of a rating, or (B) as may be necessary or desirable in order to obtain the approval of the Series 2006 Bonds by the Office of the Attorney General of the State of Texas, which changes or amendments do not, in the judgment of the City, materially adversely affect the interests of the owners of the Outstanding Parity Obligations;

(v) To make such changes, modifications or amendments as are permitted by Section 18(c)(v) of this Eighth Supplement;

(vi) To make such changes, modifications or amendments as may be necessary or desirable, which shall not adversely affect the interests of the owners of the Outstanding Parity Obligations, in order, to the extent permitted by law, to facilitate the economic and practical utilization of Credit Agreements with respect to the Parity Obligations; or

(vii) To make such other changes in the provisions hereof as the City may deem necessary or desirable and which shall not, in the judgment of the City, materially adversely affect the interests of the owners of Outstanding Parity Obligations.

Notice of any such amendment may be published by the City in the manner described in subsection (c) of this Section; provided, however, that the publication of such notice shall not constitute a condition precedent to the adoption of such amendatory ordinance and the failure to publish such notice shall not adversely affect the implementation of such amendment as adopted pursuant to such amendatory ordinance.

(b) **Amendments With Consent.** Subject to the other provisions of this Eighth Supplement, the Insurer and the owners of Outstanding Series 2006 Bonds aggregating a majority in Outstanding Principal Amount shall have the right from time to time to approve any amendment, other than amendments described in Subsection (a) of this Section, to this Eighth Supplement which may be deemed necessary or desirable by the City; provided, however, that nothing herein contained shall permit or be construed to permit, without the approval of the owners of all of the Outstanding Series 2006 Bonds, the amendment of the terms and conditions in this Eighth Supplement or in the Series 2006 Bonds so as to:

- (i) Make any change in the maturity of the Outstanding Series 2006 Bonds;
- (ii) Reduce the rate of interest borne by Outstanding Series 2006 Bonds;
- (iii) Reduce the amount of the principal payable on Outstanding Series 2006 Bonds;
- (iv) Modify the terms of payment of principal of or interest on the Outstanding Series 2006 Bonds, or impose any conditions with respect to such payment;
- (v) Affect the rights of the owners of less than all Series 2006 Bonds then Outstanding; or
- (vi) Change the minimum percentage of the Outstanding Principal Amount of Series 2006 Bonds necessary for consent to such amendment.

(c) **Notice.** If at any time the City shall desire to amend this Eighth Supplement other than pursuant to subsection (a) of this Section, the City shall cause notice of the proposed amendment to be published in a financial newspaper or journal of general circulation in The City of New York, New York, and a newspaper of general circulation in the City, once during each calendar week for at least two successive calendar weeks. Such notice shall briefly set forth the nature of the proposed amendment and shall state that a copy thereof is on file at the principal office of the Registrar for inspection by all owners of Series 2006 Bonds. Such publication is not required, however, if the City gives or causes to be given such notice in writing to each owner of Series 2006 Bonds.

(d) **Receipt of Consents.** Whenever at any time not less than thirty days, and within one year, from the date of the first publication of said notice or other service of written notice of the proposed amendment the City shall receive

an instrument or instruments executed by the Insurer and all of the owners or the owners of at least a majority in Outstanding Principal Amount of Series 2006 Bonds, as appropriate, which instrument or instruments shall refer to the proposed amendment described in said notice and which specifically consent to and approve such amendment in substantially the form of the copy thereof on file as aforesaid, the City may adopt the amendatory ordinance in substantially the same form.

(e) ***Effect of Amendments.*** Upon the adoption by the City of any ordinance to amend this Eighth Supplement pursuant to the provisions of this Section, this Eighth Supplement shall be deemed to be amended in accordance with the amendatory ordinance, and the respective rights, duties, and obligations of the City and all the owners of then Outstanding Series 2006 Bonds and all future owners of the Series 2006 Bonds shall thereafter be determined, exercised, and enforced under the Master Ordinance and this Eighth Supplement, as amended.

(f) ***Consent Irrevocable.*** Any consent given by any owner of Series 2006 Bonds pursuant to the provisions of this Section shall be irrevocable for a period of six months from the date of the first publication or other service of the notice provided for in this Section, and shall be conclusive and binding upon all future owners of the same Series 2006 Bonds during such period. Such consent may be revoked at any time after six months from the date of the first publication of such notice by the owner who gave such consent, or by a successor in title, by filing notice thereof with the Registrar and the City, but such revocation shall not be effective if the owners of a majority in Outstanding Principal Amount of Series 2006 Bonds, prior to the attempted revocation, consented to and approved the amendment.

(g) ***Ownership.*** For the purpose of this Section, the ownership and other matters relating to all Series 2006 Bonds registered as to ownership shall be determined from the Registration Books. The Registrar may conclusively assume that such ownership continues until written notice to the contrary is served upon the Registrar.

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SECTION 13. EIGHTH SUPPLEMENT TO CONSTITUTE A CONTRACT; EQUAL SECURITY. In consideration of the acceptance of the Series 2006 Bonds, the issuance of which is authorized hereunder, by those who shall hold the same from time to time, this Eighth Supplement shall be deemed to be and shall constitute a contract between the City and the Holders from time to time of the Series 2006 Bonds and the pledge made in this Eighth Supplement by the City and the covenants and agreements set forth in this Eighth Supplement to be performed by the City shall be for the equal and proportionate benefit, security, and protection of all Holders, without preference, priority, or distinction as to security or otherwise of any of the Series 2006 Bonds authorized hereunder over any of the others by reason of time of issuance, sale, or maturity thereof or otherwise for any cause whatsoever, except as expressly provided in or permitted by this Eighth Supplement.

APPENDIX C

CITY'S AUDITED FINANCIAL STATEMENTS FOR THE YEAR ENDED SEPTEMBER 30, 2005

The information contained in Appendix C consists of selected portions of the City's Annual Financial Report for the fiscal year ended September 30, 2005 selected by the City of San Antonio for inclusion herein, and is not intended to be a complete statement of the City's financial condition. Reference is made to the Comprehensive Annual Financial Report for further information.

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CITY OF SAN ANTONIO

OFFICE OF THE COMPTROLLER
SAN ANTONIO, TEXAS 78204

June 29, 2006

To the Honorable Mayor and City Council:

It is my pleasure to present the City of San Antonio's (City) Comprehensive Annual Financial Report (CAFR) for the fiscal year ended September 30, 2005. This report is published to provide the City Council, City staff, our citizens, and other readers with detailed information concerning the financial position and activities of the City.

This document was prepared and is presented by the City's Finance Department. Accordingly, City management is responsible for both the accuracy of the presented data and the completeness and fairness of the presentation, including all disclosures.

It should be noted that the public accounting firms KPMG LLP, Leal & Carter PC, and Robert J. Williams, CPA, have audited the financial statements contained herein. As reflected in the independent auditors' report, the City's financial statements are presented fairly in all material respects in accordance with U.S. generally accepted accounting principles.

The audit of the aforementioned independent auditors was also designed to meet the requirements of the Single Audit Act Amendments of 1996, Office of Management and Budget (OMB) Circular A-133, and the State of Texas Single Audit Circular. The Independent Auditors' Report on the basic financial statements, MD&A (required supplementary information), and required disclosures and schedules are included in the Financial Section of this CAFR. Required reports and schedules mandated by the Single Audit Act Amendments of 1996, OMB Circular A-133, and the State of Texas Single Audit Circular are in separate documents.

THE REPORT

The CAFR is presented in three sections: introductory, financial, and statistical.

- The introductory section contains the transmittal letter, a copy of the Government Finance Officers Association Certificate of Achievement for Excellence in Financial Reporting, the City's organizational chart, and a list of principal officials.
- The financial section includes the Independent Auditors' Report, Management's Discussion and Analysis (MD&A), the basic financial statements, which consist of government-wide and fund financial statements and notes to the financial statements, required supplementary information other than MD&A, Combining Financial Statements and other supplementary information.
- The statistical section consists of selected financial and demographic information presented on a multi-year basis.

As noted above, included in the Financial Section of the CAFR is the MD&A, which presents a narrative introduction, overview, and analysis of the basic financial statements. This transmittal letter complements the MD&A and should be read in conjunction with it. The City of San Antonio's MD&A can be found immediately following the report of the independent auditors.

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THE REPORTING ENTITY AND CITY SERVICES

The City of San Antonio is a home rule city that was incorporated in 1837 and chartered in 1951. It is structured as a Council-Manager form of government with a Mayor and ten Council Members each serving two-year terms, limited to two consecutive terms. San Antonio is located in South Central Texas, approximately 75 miles south of the state capital of Austin and serves as the county seat for Bexar County. San Antonians enjoy first-rate medical services, a convenient and efficient airport, an excellent highway system, mild weather, and superb recreation choices, including: championship golf courses, theme parks, historical attractions, museums, professional sporting attractions, and a lively performing arts environment.

As of November 30, 2005, the City's geographic area was approximately 519 square miles making it one of the largest cities in the United States. The United States Census Bureau cites the City as the second most populated city in the state of Texas and eighth most populated city in the country. The estimated population grew from 1,278,300 in fiscal year 2004 to 1,299,200 in fiscal year 2005, an increase of 1.63%.

Below are further details regarding the City as a reporting entity and public service provider.

Reporting Entity

Pursuant to the reporting standards contained in Governmental Accounting Standards Board (GASB) Statement No. 14, *The Financial Reporting Entity*, as amended by GASB Statement No. 39, *Determining Whether Certain Organizations Are Component Units – an amendment of GASB Statement No. 14*, other related entities are included in the CAFR as blended or discretely presented component units. Blended component units are those entities that are considered as part of the City's operations but are legally separate entities. Those entities are the City of San Antonio Health Facilities Development Corporation, the City of San Antonio Industrial Development Authority, the San Antonio Fire and Police Pension Fund, the San Antonio Fire and Police Retiree Healthcare Fund, the City of San Antonio Texas Municipal Facilities Corporation, the City of San Antonio Texas Starbright Industrial Development Corporation, and the City of San Antonio Texas Convention Center Hotel Finance Corporation.

Entities that require discrete presentation are the San Antonio Development Agency (SADA), the City of San Antonio Education Facilities Corporation (SAEFC), the Greater Kelly Development Authority (GKDA), the San Antonio Housing Trust Foundation, Inc. (SAHTF), the San Antonio Local Development Company, Inc. (SALDC), dba South Texas Business Fund and Brooks Development Authority (BDA), San Antonio Water System (SAWS), and City Public Service (CPS). SAWS and CPS are independently managed, municipally owned utility systems that operate under quasi-independent boards of trustees. For additional details on each of these entities and the basis for their respective presentation in our financial report, please refer to the Financial Section, Note No. 1, entitled, "Reporting Entity."

Services

The City provides a vast array of municipal services. These services include, but are not limited to, fire and police protection, street and sidewalk maintenance, libraries, parks, water and electric and natural gas services, and solid waste disposal. In addition, the City maintains preventive health services and facilitates economic and neighborhood development. These services are funded from various sources, which include ad valorem taxes, hotel/motel taxes, sales taxes, grants, user fees, revenues from municipally owned utilities, and bond proceeds.

City services are augmented through non-City agencies and local foundations such as SADA, SAEFC, SAHTF, and SALDC.

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ECONOMIC CONDITIONS AND OUTLOOK

As a community, San Antonio has positioned itself for long-term growth and prosperity by successfully following a strategy to diversify its economy and improve quality-of-life for all citizens. City government has played an integral part by implementing "A Strategic Plan for Enhanced Economic Development" through the collaborative efforts of San Antonio, Inc., a group of economic development organizations within San Antonio.

The City's economic plan promotes further development of San Antonio's major industries, which include biomedical research and health services, international trade and distribution, information technology and security, telecommunications, aerospace, tourism, financial services, automotive manufacturing, and the military. Untapped economic opportunities are also a part of the City's economic development plan.

The City is also undertaking ongoing infrastructure improvements, neighborhood revitalization, and workforce development initiatives, as well as providing assistance and attraction programs that are geared to businesses of all sizes. Both government and citizens are actively committed to increasing the caliber of educational and economic opportunities, expanding arts and leisure choices, revitalizing older neighborhoods, and planning for overall growth in San Antonio.

The North American Free Trade Agreement (NAFTA) has enabled the City to capitalize on international trade opportunities by becoming a distribution point and center for companies doing business in Mexico. San Antonio is the closest major U.S. city to Mexico's biggest markets and enjoys close cultural and business ties to that nation.

Following are additional details that provide a more in-depth look at the business climate and local economy for the City of San Antonio.

Business Climate and Local Economy

San Antonio's healthy economy and positive business climate are enhanced by elements key to continued economic growth, such as an advanced telecommunications system, enhanced opportunities for higher education, and strong workforce development programs. Also enhancing San Antonio's business appeal is the high quality-of-life the City offers and a cost-of-living that is well below the national average. Below is a brief discussion on the City's local economic development activities that will help to ensure its economic sustainability and viability.

KellyUSA

KellyUSA, a former U.S. Air Force Base, Greater Kelly Development Authority is transforming the base into an inland port with highway, rail and air access, and positioning the development authority as a multi-modal international port. As of December 2005, there were 63 tenants (commercial companies and federal agencies), employing over 12,469 people with an average salary of over \$38,000, and a total economic impact of \$2.76 billion per year. Major commercial employers at KellyUSA include Boeing, Lockheed Martin, General Electric, General Dynamics, Standard Aero, Pratt & Whitney, Chromalloy, Gore Design Completions, and EG&G.

With 95 percent of the marketable 8.2 million square feet leased, GKDA is now focused on development of new Class A facilities leveraging public and private investment to create more jobs for San Antonio. In 2005, a total of 514,400 square feet of new hangar, distribution and flex/office facilities were constructed at KellyUSA. GKDA's development plan forecasts \$366 million of new construction for buildings and infrastructure over the next five years. KellyUSA's economic impact to San Antonio is projected to increase to over \$4.6 billion per year upon full build-out.

Brooks City-Base

Brooks City-Base remains open for business, although the military missions will be relocated over the next three to five years as a result of the 2005 Base Realignment and Closure (BRAC) process. As it stands, San Antonio is at least three years ahead in redevelopment over other installations across the nation facing the same news from

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ECONOMIC CONDITIONS AND OUTLOOK (Continued)

Brooks City-Base (Continued)

BRAC. Despite the BRAC outcome, Brooks City-Base is moving toward sustainability starting with Brooks Technology & Business Park, which was officially established on July 22, 2002. A Tax Increment Reinvestment Zone has been created that encompasses the area inside and outside of Brooks City-Base, providing for yet another tool to assist in the development of Brooks City-Base and the surrounding area. Currently, there are over \$170 million worth of projects planned for or already under way at Brooks City-Base.

In 2005, the BDA and local major pharmaceutical company, DPT Laboratories, approved an 18-year build-to-suit lease agreement for a combination research and development (R&D) warehouse and production facility of nearly a quarter-million square feet at Brooks City-Base. The project involves a capital investment of \$24 million and construction is under way on the two new major buildings at Brooks City-Base. Additionally, Vanguard Health Systems, Inc., and its affiliate Baptist Health System (BHS), announced in 2005 that BHS has signed a letter of intent to acquire land to relocate Southeast Baptist Hospital to Brooks City-Base. The new hospital will bring 700 to 800 jobs to the South Side and represents a significant economic investment in the community. The City and County are also planning to construct a \$24.5 million new Emergency Operation Center at Brooks. Also, San Antonio Metropolitan Public Health has completed renovation of a Brooks City-Base facility to establish a BioSafety Level 3 Laboratory. Additionally, the State Board of Education approved the charter school application filed by Somerset Academy in collaboration with the Brooks City-Base Foundation (BCBF) and the BDA, allowing for the development of a charter school at Brooks City-Base. Brooks City-Base is on the move, gaining momentum and generating new energy to attract science and technology tenants and fully develop the area in and around Brooks City-Base.

Fort Sam Houston

Fort Sam is engaged in military-community partnership initiatives to help reduce infrastructure costs and pursue asset management opportunities using military facilities. In April 2000, the United States Army (the Army) entered into a partnership with the private organization, Fort Sam Houston Redevelopment Partners, Ltd. (FSHRP), for the redevelopment of the former Brooke Army Medical Center (BAMC) and two other buildings at Fort Sam. These three buildings, totaling about 500,000 square feet in space and located in a designated historic district, had been vacant for some time and were in a deteriorating condition. On June 21, 2001, FSHRP signed a 50-year lease with the Army to redevelop and lease these three properties to commercial tenants.

In September 2003, the Army relocated Army South Headquarters from Puerto Rico to Fort Sam, bringing approximately 500 new jobs to San Antonio with an annual economic impact of approximately \$200 million. The Army negotiated a lease with the FSHRP to locate U.S. Army South and the Southwest Region Installation Management Agency in the newly renovated historic facilities in the summer of 2004. The continued success of this unique public-private partnership at Fort Sam is critical to assisting the Army in reducing infrastructure support costs, preserving historical assets, and promoting economic development opportunities. The Army intends to extend the public-private partnership initiative to include other properties at Fort Sam currently available for redevelopment.

Base Realignment and Closure (BRAC)

The recommendations of the BRAC Commission became law on November 8, 2005. As a result of BRAC, the San Antonio area will benefit from a net gain of about 3,600 jobs over the next three to five years. Transformation is ongoing throughout the military services resulting in the reorganization of many military missions and units. The Army's transformation actions at Fort Sam are expected to create approximately 1,000 jobs over the next couple of years, in addition to the increase in jobs from BRAC. The National Security Agency has also announced an expansion of its activities in San Antonio and will be adding about 1,500 jobs over the next couple of years.

Key elements of BRAC include the creation of a Department of Defense (DOD) Regional Medical Center at the new Brooke Army Medical Center (BAMC) and the establishment of Fort Sam Houston as the home of DOD enlisted medical training. BAMC will be one of only two such DOD Regional Medical Centers in the country and will merge with the Wilford Hall Medical Center (WHMC) at Lackland Air Force Base. While the WHMC

ECONOMIC CONDITIONS AND OUTLOOK (Continued)

Base-Realignment and Closure (BRAC) (Continued)

facility at Lackland will close, the DOD intends to build a new 450,000 square foot medical care clinic at Lackland. A number of Army Agency Headquarters will also be relocating to Fort Sam from other bases around the country. As these changes occur over the next three to five years, Fort Sam Houston will grow by over 10,000 jobs to about 45,000. Based on the planned changes at Fort Sam and Lackland, the community is also expecting to benefit from over \$2 billion in new construction and renovation of facilities at both bases. Finally, the recommended BRAC enhancements to military medical care training and capacity will also greatly strengthen and grow the currently existing partnerships between the military and community institutions that will facilitate continued growth in the community's targeted industry of bioscience and healthcare.

San Antonio Technology Accelerator Initiative (SATAI)

SATAI is a targeted economic development initiative focused on developing an advanced technology economy in the San Antonio region. SATAI's mission is to accelerate the regional technological economy through providing hands-on development of advanced technology start-up companies and assisting established companies in accessing tech-based solutions through Enterprise Services. One of the largest SATAI projects is the coordination of several homeland security initiatives through its leadership of the Southwest Enterprise for Regional Preparedness. SATAI's efforts in this area will lead to several state of the art technologies that will be commercialized through new start-up technology companies. SATAI has been very successful in becoming a key component in the development of San Antonio's advanced technology economy.

Aerospace Industry Development

The aerospace industry's annual economic impact to the City is approximately \$2.9 billion. This industry provides over 8,200 jobs, with employees earning annual wages totaling over \$320 million. The aerospace industry continues to expand as the City leverages its key aerospace assets, which include San Antonio International Airport, Stinson Municipal Airport, KellyUSA, Brooks City Base, Randolph AFB, Lackland AFB, and various training institutions. Many of the major aerospace industry leaders have significant operations in San Antonio, such as Boeing, Lockheed Martin, General Electric, Pratt & Whitney, Raytheon, Cessna, San Antonio Aerospace -- a division of Singapore Technologies, Southwest Airlines, American Airlines, Delta, Continental, FedEx, UPS, and others. The industry in San Antonio is very diversified with continued growth in air passenger service, air cargo, maintenance repair and overhaul (MRO), and general aviation.

San Antonio International Airport (SAT) added four new non-stop passenger routes during Fiscal Year 2005 for a total of 31 destinations, which does not include seasonal charter service to Mexico available during the spring and summer. Seven additional new non-stop flights have been announced to start during the first quarter of 2006. SAT is currently developing construction plans for a new 3,000 space parking garage and Terminals B and C, with groundbreaking expected, respectively, in the spring and summer of 2006. SAT is also in the process of an Environmental Assessment for implementation of proposed airfield capacity enhancement projects recommended in the Airport Master Plan. Stinson Municipal Airport is at 100.0% occupancy rate and has a tenant waiting list for the facilities. A Master Plan for Stinson was approved by the City Council in October 2002. Implementation of the Master Plan recommendations is currently in process pending the successful completion of an Environmental Assessment for certain airfield improvements. Groundbreaking is planned during the first quarter of 2006 for the Expanded Terminal and Office Facility Project. At KellyUSA, the MRO business is strong as tenants such as Boeing and Lockheed Martin continue to secure long-term government contracts. KellyUSA is also working to add air cargo activity as recommended by the Air Cargo Study and Strategic Plan completed in June 2002. This study also provided San Antonio International Airport with an Air Cargo Strategic Plan that includes recommendations on expanding the existing integrator service primarily provided by UPS, FedEx, and Airborne Express. Additionally, Brooks Air Force Base 311th Human Systems Wing's School of Aerospace Medicine, conducts research related to human effectiveness in aviation and is opening a new aircraft sustainability laboratory that will conduct research and development applicable to commercial aviation.

ECONOMIC CONDITIONS AND OUTLOOK (Continued)

Downtown Development Projects

2005 was a landmark year for downtown development. La Cascada, a 150-unit high-end condominium project opened its door and is near capacity. Construction has begun on a second tower adjacent to the first. In November, a new 265 all-suites hotel, La Contessa, opened its doors on the Riverwalk. During 2005, renovation of the Alamo Bank Building began on the flagship Drury Plaza Hotel. Financing of the hotel was partially funded by Empowerment Zone Facility Bonds. In addition to the hotel, Drury Southwest has partnered to renovate the Aztec Theatre building into a state of the art multimedia theatre experience. Drury is also providing, at its own expense, the final linkage to complete the downtown Riverwalk on the main channel of the San Antonio River. The Riverwalk linkage has an expected completion date of summer of 2006. The 300-room, limited service hotel is expected to open in the fall of 2006.

Earlier in the year, construction was completed on a 350-room La Quinta hotel near the convention center. In the summer ground was broken for a new 1,000-room convention center hotel adjacent to the recently remodeled Henry B. Gonzalez Convention Center. The amount of \$130 million in Empowerment Zone Facility Bonds were used to help finance the project. In addition to the hotel, 120 condominiums and an underground parking facility will also be included in the project.

Adjacent to the convention center on the Hemisfair property, a Master plan was approved to develop the area with more green space and encourage neighborhood utilization. Response from stakeholders was very positive. In accordance with the Plan, a land swap was completed with UTSA, which gave up ownership of the property that houses the Institute of Texas Cultures for space near their downtown campus to develop additional instructional buildings.

International Trade

The International Affairs Department was created to provide a clear entrance or "front door" to City programs and services in order to attract and promote trade and foreign investment, and to establish San Antonio as the "Center of the Americas." In doing so, it has identified and interfaced with over 500 local companies that do business internationally.

During fiscal year 2005, the International Affairs Department worked with 75 protocol delegations and 78 business/trade delegations that included a total 1,881 delegates that visited San Antonio. This accounted for \$1.7 million in direct expenditures by official guests in San Antonio. The department also assisted more than 600 business clients, generating over \$34 million in bilateral trade between San Antonio and Mexico.

As of November 30, 2005, the North American Development Bank (NADB) is participating in the development and financing of 90 environmental infrastructure projects with approximately \$703.8 million in loans and grants. These projects are estimated to cost a total of \$2.35 billion to build, and will benefit an estimated 7.8 million border residents throughout the 10 states that comprise the U.S.-Mexico border region.

NADB has been the catalyst to significant and unprecedented levels of investment in environmental infrastructure along the U.S.-Mexico border. NADB participation represents about 30% of the total investment in these projects. Of these, 35 have been completed, 50 are currently under construction or in various stages of completion and 13 are in the design or bidding stage. In the area of local capacity building, NADB to date has authorized technical assistance for 192 projects in 92 communities on both sides of the border.

The Free Trade Alliance San Antonio, through its International Business Development Center is an incubator program for foreign companies. As of the fourth quarter of 2005, they had 29 companies enrolled in their program. The economic impact of these companies is over \$1.5 million for the year.

International Outlook

The International Affairs Department continues to develop the Export Leaders Program that focuses on San Antonio companies with a high potential and strong commitment to develop and expand international markets. The San Antonio Export Leaders Program offers the tools, training, consultation, and coaching necessary for

ECONOMIC CONDITIONS AND OUTLOOK (Continued)

International Outlook (Continued)

companies to be successful in exporting, and offers the participants the availability to grow their company internationally. This cutting edge program has graduated 66 companies and generated \$24 million in trade in 2004. San Antonio continues to develop itself as an INLAND PORT for imports and exports to/from Mexico, China, Japan, Spain, Latin America and other regions of the world. This encompasses transportation, manufacturing and logistics facilities, professional services and value-added services involved in producing, marketing, and moving freight within the San Antonio region. In 2004-2005, the International Affairs Department worked through their foreign offices in Mexico on a logistic survey that focused on potential foreign investment prospects in San Antonio. It has identified over 50 potential leads. Over the past 13 years, the City of San Antonio has operated three commercial trade offices in Mexico: Mexico City, Guadalajara, and Monterrey which has generated over \$100 million in bilateral trade since its inception. For over 20 years, the International Affairs Department has operated a trade representative in Japan attracting multi-million dollar operations to San Antonio including Takata Seat Belt, Sony Corporation, Mycom International, Hyatt Hill Country Resort (a major Japanese investment joint venture), Colin Medical Equipment and Toyota, to name a few.

The City's commitment to international trade is evidenced in the City's International Center which houses the North American Development Bank, International Conference Center, The Trade Commission of Mexico, Foreign Commercial State Offices for Mexico and Spain, the Free Trade Alliance San Antonio, the U.S. Department of Commerce, the City's International Affairs Department, and the Convention & Visitors Bureau.

Hospitality Industry

The City's diversified economy includes a significant sector relating to the hospitality industry, which ranks second in its local economic impact. A recent study by the Greater San Antonio Chamber of Commerce found that the hospitality industry had an economic impact of nearly \$7.2 billion. The estimated annual payroll for the industry was \$1.2 billion, and the industry employed over 80,000. The economic impact study is scheduled for update in 2006.

San Antonio tourism attracts over 21.3 million visitors with direct spending across all industries in the City of \$4.3 billion and ranked tenth among U.S. destinations for overnight leisure travel, according to the National Performance Monitor survey conducted by D.K. Shifflet & Associates. The list of attractions in the San Antonio area includes among many others, the Alamo, (and other sites of historic significance), the River Walk, two major theme parks (SeaWorld of Texas and Six Flags Fiesta Texas), and the professional basketball team, the San Antonio Spurs. San Antonio is also one of the top convention cities in the country. The City is proactive in attracting convention business through its management practices and marketing efforts.

In 2004, the City's overall performance for hotel occupancy increased by 1.5%. Revenue per available room ("REVPAR") increased by 4.4%, and total room nights sold in the destination increased by 2.1%. In 2005, from January through November, hotel occupancy increased by 6.5%, REVPAR increased by 12.3%, and total room nights sold in the destination increased by 7.8%, as compared to the same prior period in 2004.

FINANCIAL INFORMATION

Accounting System and Budgetary Control

The City's accounting system supports an adequate internal control structure. The structure helps to safeguard the City's assets against loss, theft, or misuse. The accounting system provides reliable financial records for preparing financial statements in conformity with U.S. generally accepted accounting principles. The internal control structure provides reasonable, but not absolute, assurance that the City's assets are safeguarded. The concept of reasonable assurance first recognizes that the cost of a control should not exceed the benefits likely to be derived. Secondly, the evaluation of costs and benefits requires estimates and judgments by management.

FINANCIAL INFORMATION (Continued)

Accounting System and Budgetary Control (Continued)

Budgetary compliance is a significant tool for managing and controlling governmental activities, as well as ensuring conformance with the City's budgetary limits and specifications. The objective of budgetary controls is to ensure compliance with legal provisions embodied in the annual appropriated budget approved by City Council. Levels of budgetary control, that is the levels at which expenditures cannot legally exceed appropriated amounts, are established by function and activity within individual funds. The City utilizes an encumbrance system of accounting as one mechanism to accomplish effective budgetary control. Encumbered amounts lapse at year-end, these same encumbrances are generally appropriated as part of the following year's budget. For the fiscal year ending September 30, 2004, the Government Finance Officers Association of the United States and Canada (GFOA) presented an award of Distinguished Budget Presentation to the City.

As demonstrated by the statements and schedules in the Financial Section of this report, the City continues to meet its responsibility for sound financial management. As in the Financial Section, all monetary amounts presented in the remainder of this letter are expressed in thousands, except where noted.

Fiscal Management and Administrative Topics

Pension and Postemployment Retirement Benefits

The City provides pension retirement benefits for its eligible employees through two plans. For uniformed Fire and Police employees, retirement benefits are provided through the Fire and Police Pension Fund, a single-employer defined benefit retirement plan. Contribution and benefit levels are established under State statute. For fiscal year 2005, active members contributed 12.3% of covered payroll, or \$24.9 million and the City contributed 24.6% or \$49.7 million.

The City provides all other eligible employees, exclusive of fire and police employees, retirement benefits through the Texas Municipal Retirement System (TMRS), a nontraditional, joint contributory, hybrid defined benefit plan. TMRS is a statewide agent multiple-employer public employee retirement system. Contributions to the system are actuarially determined. The required contribution from City employees is 6.0%, while the City matches at a rate of approximately 12.5%. Both the City and its covered employees made the required contributions of \$25.13 million and \$12.32 million, respectively. For additional information on the City's pension plans, see Note 8 in the notes to the financial statements.

With respect to postemployment health benefits, the City provides benefits for all non-uniformed City retirees and for all pre-October 1, 1989 uniformed fire and police retirees. The cost of the program is reviewed annually and actuarially determined costs of medical claims are funded jointly on a pay-as-you-go basis with the City contributing 2/3 and the retirees contributing 1/3 of the cost. As of September 30, 2005, there were 1,301 retirees participating in the program and currently there are 6,060 active civilian employees who may become eligible for this program in the future.

The second postemployment health benefit program provides retirement healthcare benefits for eligible fire and police retirees under the Fire and Police Retiree Healthcare Fund (Fund). Contribution and benefits levels are established under the City's collective bargaining agreements with the Fire and Police Unions, respectively. The benefits of this plan are financed on a prefunded basis. For fiscal year 2005, the City contributed \$17.2 million to the Fund and active employees and retirees contributed \$3.3 million. For additional information on the City's post-employment health benefits, see Note 9 of the notes to the financial statements.

Employee Benefits Program

The City's Self-Insurance Fund continues to experience increased expenses due to rising healthcare costs, increased prescription drug costs, increased claims volume, and changing employee demographics. The City continues to focus on cost containment programs such as hospital audits, hospital pre-certification, utilization review, large case management, prescription benefit management, disease management and a preferred provider organization to assist in managing the rising cost of medical care. Such strategies have been effective for the City

FINANCIAL INFORMATION (Continued)

Fiscal Management and Administrative Topics (Continued)

Employee Benefits Program (Continued)

In managing medical costs in a changing healthcare industry. In addition to continuing the enhancement of these cost containment programs, the City engaged in a contract with a benefit consultant, The Hay Group, in 2005 to perform a comprehensive review of the Employee Benefits Program. The Hay Group, with the assistance of City staff, developed approaches to further reduce cost by developing a partnership-strategy between the City, employees, and retirees to manage healthcare costs with the goal of lowering healthcare spending by maintaining premium levels while increasing deductibles and out-of-pocket (OPP) maximums in conjunction with the funding of flexible spending accounts. Maintaining 2005 premiums and co-insurance levels through 2006 allows time to engage in the upcoming negotiations with the Police & Fire associations. The total cost savings projected for fiscal year 2006, as a result of the program changes with no premium increase for civilian active and retirees, is estimated at \$1.1 million. In fiscal year 2005, the Employee Benefits Fund had cash and investment in reserve of \$3.5 million and a negative net assets balance of \$20.69 million. For additional information on the City's risk and employee benefit programs, see Note 12 of the notes to the financial statements.

Risk Management Programs

For fiscal year 2005, the Insurance Reserve Fund maintained a positive net assets balance of \$3.61 million. The Workers' Compensation Fund reflected a negative net assets balance of \$4.25 million for fiscal year 2005. The Insurance Reserve and Workers' Compensation Funds carried cash reserves as of September 30, 2005 in the amount of \$16.42 million and \$9.76 million, respectively.

The City's Liability and Workers' Compensation Self-Insurance Funds operate under the direction of the Risk Management Division within the Human Resources Department. Programs are reviewed continuously to reduce liability exposure, minimize losses, and strategize to reduce the frequency of injuries and illnesses, and the cost of workers' compensation.

Appropriate insurance policies are purchased by the City to cover standard risks associated with commercial property coverage for its buildings, airport liability, boilers and machinery, commercial crime, medical professional insurance, and public official bonds. Excess insurance policies are also purchased to cover large liability and workers' compensation exposures.

In addition, the City engages an actuary to review the City's self-insurance funds. Such reviews estimated outstanding losses, project the ultimate losses and recommend overall funding each year. Contributions to the City's self-insurance funds include: department assessments from the general fund, special revenue funds, and other proprietary funds.

Cash and Investment Management

The City's investment policies are governed by state statute and the City's own written investment policies. Under Texas law, the City is required to invest its funds under written investment policies that primarily emphasize safety of principal and liquidity, investment diversification, yield, maturity, and the quality and capability of investment management. This includes a list of authorized investments for City funds, maximum allowable stated maturity of any individual investment, and the maximum average dollar-weighted maturity allowed for pooled fund groups. All City funds must be invested consistent with a formally adopted "investment strategy statement" that specifically addresses each fund's investment. Each investment strategy statement will describe strategy objectives concerning: (1) suitability of investment type, (2) preservation and safety of principal, (3) liquidity, (4) marketability of each investment, (5) diversification of the portfolio, and (6) yield.

The City is authorized to use demand accounts, time accounts, certificates of deposit, and other permissible investments including obligations of the U.S. Treasury and U.S. Agencies, obligations of States and Cities, Commercial Paper, Repurchase Agreements, Money Market Funds, and Investment Pools. The City's investment portfolio does not include callable obligations or any derivative products. It is not the City's policy to use derivative products in its portfolio, nor does the City leverage its investments. At September 30, 2005, at fair

FINANCIAL INFORMATION (Continued)

Fiscal Management and Administrative Topics (Continued)

Cash and Investment Management (Continued)

value, City investment funds were 92.0% invested in obligations of the United States, or its agencies and instrumentalities, and 6.9% invested in a money market mutual fund, with the weighted average maturity of the portfolio being less than one year. The remaining 1.1% of the City's portfolio includes the Convention Center Debt Service Reserve Fund of \$8.5 million, which was invested in a fully collateralized repurchase agreement that is fully secured by obligations of the United States or its agencies and instrumentalities. The investments and maturity terms are consistent with State law, and the City's investment policy. For additional information on Cash and Investments, see Note 3 of the notes to the financial statements.

Debt Administration

The City utilizes a comprehensive debt management financial planning program (The Debt Management Plan), which is updated annually. The Debt Management Plan is a major component of the City's financial planning. The model projects financing needs while measuring and assessing the cost and timing of each debt issuance. It involves comprehensive financial analysis which utilizes computer modeling, and incorporates variables such as interest rate sensitivity, assessed values changes, annexations, and current ad valorem tax collection rates. Use of this financial management tool has assisted the City in meeting its financing needs by facilitating timely and thorough planning which has allowed the City to capitalize on market opportunities.

Strict adherence to conservative financial management has allowed the City to meet its financing needs while at the same time maintaining its "Aa2", "AA+" and "AA+" bond rating by Moody's Investors Service, Inc. (Moody's), Standard & Poor's Public Ratings Services, a division of McGraw-Hill Corporation (S&P), and Fitch Ratings, Inc. (Fitch), respectively. For additional information on the City's long-term debt, see Note 6 of the notes to the financial statements.

OTHER INFORMATION

Independent Audit

State statutes require that an annual audit by an independent certified public accountant be conducted. The City selected the accounting firms KPMG LLP, Leal & Carter PC, and Robert J. Williams, CPA in 2002. In addition to meeting the requirements set forth in State statutes, the audit was also designed to meet the requirements of the Single Audit Act Amendments of 1996 and related OMB Circular A-133. The Independent Auditors' Report on the basic financial statements, management's discussion and analysis (required supplementary information), required disclosures and schedules are included in the Financial Section of this CAFR. The Independent Auditors' Report along with other required reports and schedules mandated by the Single Audit Act Amendments of 1996 and OMB Circular A-133 and the State of Texas Audit Circular are in a separate document.

Awards

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the City for its CAFR for the fiscal year ended September 30, 2004. This was the 29th consecutive year that the government has achieved this prestigious award. In order to be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized CAFR. This report must satisfy both U.S. generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe that our current comprehensive annual financial report continues to meet the Certificate of Achievement Program's requirements and we are submitting it to the GFOA to determine its eligibility for another certificate.

OTHER INFORMATION (Continued)

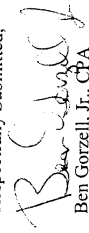
Awards (Continued)

The San Antonio Planning Department has recently received both national and state recognition. The International City/County Management Association recognized the Community Building and Neighborhood Planning Program in 2005 for Excellence in Citizen Involvement. In 2004, the Texas Chapter of the American Planning Association also honored the City of San Antonio's Planning Department with two awards: the Current Planning Award for the Flex Zoning Districts in conjunction with the Southside Initiative, and the Project Planning Award for the River Improvement Overlay District.

The City of San Antonio Development Services Department was recognized by Hansen as its Outstanding Power User Survey Award for the department's use of online permitting and inspection scheduling which is one of the highest in the nation.

The preparation of the City of San Antonio, Texas Comprehensive Annual Financial Report for the fiscal year ended September 30, 2005, was made possible by the dedication and hard work of the Finance Department, particularly the staff of the Accounting Division. Each member of the Department has my sincere appreciation for their contributions to the preparation of this document. In closing, please accept my sincere gratitude to the Mayor and City Council, City Manager, Deputy City Managers, Assistant City Managers, Assistant to the City Manager, and their staff, for their continued support.

Respectfully Submitted,


Ben Gorzell, Jr., CPA

Director

Finance Department

Certificate of Achievement for Excellence in Financial Reporting

Presented to

City of San Antonio,
Texas

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
September 30, 2004

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



Carla E. Perry

President

Jeffrey R. Enen

Executive Director

CITY COUNCIL

- BOARD & COMMISSIONS**
- CITY CLERK**
- CITY MANAGER**
 - CITY AUDITOR**
 - MUNICIPAL COURT JUDGES**
 - City Attorney**
 - Municipal Integrity**
 - Assistant to the City Manager**
 - Alamodome
 - Aviation
 - Convention & Visitors Bureau
 - Convention Facilities
 - Cultural Affairs
 - Deputy City Manager *Vacant*
 - Assistant City Manager**
 - Community Initiatives
 - Human Resources
 - International Affairs
 - Library (L)
 - Metropolitan Health District
 - Assistant City Manager**
 - Environmental Services
 - Finance
 - Fire & Police Pension Board (L)
 - Fire & Police Retiree Health Board (L)
 - Municipal Courts
 - Public Utilities
 - Public Works
 - VIA (L)
 - Assistant City Manager**
 - Development Services
 - External Relations
 - Fire/EMS Emergency Mgmt.
 - Parks & Recreation
 - Police
 - Assistant City Manager**
 - Council Action Team
 - Economic Development
 - Code Compliance
 - Housing & Community Development
 - Neighborhood Action
 - Planning
 - Assistant City Manager/CIO**
 - Customer Service/311
 - Information Technology
 - ERM Project
 - Purchasing & General Services
 - Assistant to the City Manager**
 - Asset Management
 - Contract Services
 - Management & Budget
 - Mayor & Council Support

Legend:

- Electable Officials** (Diamond shape)
- Appointed Officials** (Hexagon shape)
- Departments** (Rectangle shape)
- Positions** (Dashed line shape)

CITY OF SAN ANTONIO, TEXAS

Incorporated December 14, 1837

Charter Adopted October 2, 1951

Council - Manager Form of Government

CITY COUNCIL

Phil Hardberger, Mayor

Roger O. Flores

Sheila D. McNeil

Roland Gutierrez

Richard Perez

Patti Radle

Delicia Herrera

Elena Guajardo

Art A. Hall

Kevin A. Wolff

Christopher “Chip” Haass

CITY MANAGER

Sheryl L. Sculley

DEPUTY CITY MANAGER

Jelynn LeBlanc Burley

DEPUTY CITY MANAGER

Pat DiGiovanni

ASSISTANT CITY MANAGER

Michael Armstrong

ASSISTANT CITY MANAGER

Frances A. Gonzalez

ASSISTANT CITY MANAGER

Erik J. Walsh

ASSISTANT TO THE CITY MANAGER

Roland A. Lozano

**MEMBER OF THE GOVERNMENT FINANCE OFFICERS
ASSOCIATION OF THE UNITED STATES & CANADA**

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***City of San Antonio
Texas***

Financial Section

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***City of San Antonio
Texas***

Independent Auditors' Report

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300 Convent, Suite 1200
San Antonio, TX 78205



Robert J. Williams
Certified Public Accountant
1100 N.W. Loop 410, Suite 700
San Antonio, TX 78213

LEAL & CARTER, P.C.

CERTIFIED PUBLIC ACCOUNTANTS
11122 Wurzbach Rd. / Suite 200
San Antonio, TX 78230-2573

Independent Auditors' Report

The Honorable Mayor
and Members of City Council
City of San Antonio, Texas:

We have jointly audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of San Antonio, Texas, as of and for the year ended September 30, 2005, which collectively comprise the City of San Antonio, Texas' basic financial statements as listed in the accompanying table of contents under "Basic Financial Statements." These financial statements are the responsibility of the City of San Antonio, Texas' management. Our responsibility is to express opinions on these financial statements based on our audit. We did not jointly audit the financial statements of certain discretely presented component units and blended component units included in the governmental and fiduciary funds of the City of San Antonio, Texas, which represent the indicated percent of total assets and total revenues as presented in the table below. Those financial statements were audited by other auditors, including KPMG LLP, Robert J. Williams, CPA, and Leal & Carter, P.C., acting separately, whose reports thereon have been furnished to us, and our opinions, insofar as they relate to the amounts included for those component units, are based solely on the reports of the other auditors.

	Percent not jointly audited	
	Total assets	Total revenue
Government-wide		
Governmental activities	0%	0%
Business-type activities	0%	0%
Discretely presented component units	100%	100%
Fund statements		
Major funds	0%	0%
Aggregate remaining fund information	75%	35%

	Percent audited by KPMG separately		Percent audited by Leal & Carter separately		Percent audited by Robert J. Williams separately	
	Total assets	Total revenue	Total assets	Total revenue	Total assets	Total revenue
Government-wide						
Discretely presented component units	71%	79%	1%	2%	71%	79%
Fund statements						
Aggregate remaining fund information	0%	0%	6%	4%	0%	0%

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the City of San Antonio, Texas' internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the reports of the other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of San Antonio, Texas, as of September 30, 2005, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in conformity with U.S. generally accepted accounting principles.

The City of San Antonio, Texas adopted the provisions of Government Accounting Standards Board (GASB) Statement No. 40, *Deposit and Investment Risk Disclosures, an Amendment to GASB Statement No. 3*, as of September 30, 2005.

The Management's Discussion and Analysis on pages 1 through 12, the Budgetary Comparison Schedule on page 129, and Schedules of Funding Progress on page 130 are not required parts of the basic financial statements, but are supplementary information required by U.S. generally accepted accounting principles. We, and the other auditors, have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we, and the other auditors, did not audit this information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of San Antonio, Texas' basic financial statements. The introductory section, the combining financial statements, schedules and other supplementary information, and statistical section are presented for purposes of additional analysis and are not required parts of the basic financial statements. The combining financial statements and schedules and other supplementary information have been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and, in our opinion, based on our audit and the reports of other auditors, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory section and statistical section have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

KPMG LLP Robert Williams CPA Seal & Carter, P.C.

June 28, 2006



***City of San Antonio
Texas***

***Management's Discussion and Analysis
(Required Supplementary Information)
(Unaudited)***

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MANAGEMENT'S DISCUSSION AND ANALYSIS

The City of San Antonio (City) presents the following discussion and analysis of the City's financial performance during the fiscal year ended September 30, 2005. This discussion and analysis is intended to assist readers in focusing on significant financial issues and changes in the City's financial position, and identifying any significant variances from the adopted budget. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in our letter of transmittal and the financial statements provided in this report. All amounts, unless otherwise indicated, are expressed in thousands of dollars.

Financial Highlights

- The assets of the City exceeded its liabilities by \$2,517,663 (net assets). Of this amount, \$134,771 (unrestricted net assets) may be used to meet the government's ongoing obligations to citizens and creditors.
- As of the end of the current fiscal year, the City's governmental funds reported combined ending fund balances of \$772,954, an increase of \$236,226 compared to the fiscal year 2004 fund balance. The total unreserved fund balance of \$573,286 is available for spending at the government's discretion. Of this amount, \$40,860 is designated and \$532,426 is undesignated fund balance.
- At the end of the current fiscal year, unreserved fund balance for the General Fund was \$107,490 or 18.5% of the total General Fund expenditures.

Overview of the Financial Statements

This discussion and analysis is intended to serve as the introduction to the City of San Antonio's basic financial statements which are comprised of three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements.

Government-wide Financial Statements

The government-wide financial statements are designed to provide readers with a broad overview of the City's finances, in a manner similar to private-sector business financial presentation.

The *statement of net assets* is a presentation of the City's assets and liabilities, including capital and infrastructure assets, and long-term liabilities. This statement reports the difference between assets and liabilities as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the City is improving or deteriorating.

The *statement of activities* presents information showing how the government's net assets changed during the fiscal year. Changes in net assets are recorded when the underlying event giving rise to the change occurs regardless of the timing of the cash flows. Therefore, revenues and expenses reported in this statement for some items will not result in cash flows until future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave). Both of the government-wide financial statements distinguish functions of the City that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees or charges (business-type activities). Governmental activities include general government, public safety, public works, sanitation, health services, culture and recreation, convention and tourism, conservation, urban redevelopment and housing, welfare and economic development opportunity. The business-type activities of the City include the airport system, parking system, and environmental services.

In addition, the basic financial statements provide information regarding the City's legally separate discretely presented component units. Component unit financial information is reported separately from the primary government in the government-wide financial statements.

(amounts are expressed in thousands)

Fund Financial Statements

The accounts of the City are organized on the basis of funds, each of which is considered a separate accounting entity. Government resources are allocated to and accounted for in individual funds based upon the purposes for which they are to be spent and the means by which spending activities are controlled.

Fund financial statements are used to present financial information detailing resources that have been identified for specific activities. The focus of the fund financial statements is on the City's major funds, although non-major funds are also presented in aggregate and further detailed in the supplementary statements. The City uses fund accounting to ensure and demonstrate compliance with requirements placed on resources. Funds are divided into three categories: governmental, proprietary, and fiduciary. Fund financial statements allow the City to present information regarding fiduciary funds, since they are not reported in the government-wide financial statements.

Governmental funds. Governmental funds are used for essentially the same functions reported in the governmental activities in the government-wide financial statements. However, unlike the government-wide statement, governmental fund financial statements focus on the near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

As the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented in the governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental fund and governmental activities.

The City of San Antonio maintains five individual governmental fund types for financial reporting purposes. The governmental fund types are General Fund, Special Revenue Funds, Capital Projects Funds, Debt Service Funds, and Permanent Funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the general fund, Convention Center Hotel Finance Corporation Fund and the debt service funds, all of which are considered to be major funds. Data from the other funds is combined into a single, aggregated presentation labeled "Nonmajor Governmental Funds." Individual fund data for each non-major governmental fund is provided in the form of combining statements elsewhere in this report.

Proprietary funds. The City maintains two types of proprietary funds. *Enterprise funds* are used to report the functions presented in business-type activities in the government-wide financial statements. The City uses enterprise funds to account for its airport, parking, and environmental services funds. *Internal service funds* are used to accumulate and allocate costs internally among the City's various functions, including, self-insurance programs, other internal services and information technology services. The services provided by these funds predominantly support the governmental rather than the business-type functions. They have been included within the governmental activities in the government-wide financial statements that are reported alongside the business activities.

Proprietary fund financial statements provide separate and more detailed information for the airport, parking, and environmental services funds. The airport and parking funds are considered major funds of the City while internal service funds are combined into a single aggregated presentation in the proprietary fund financial statements.

Fiduciary funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the primary government. Fiduciary funds are not reflected in the government-wide financial statements as the resources of those funds are not available to support the City's programs and operations. The accounting for fiduciary funds is much like that used for the proprietary funds.

(amounts are expressed in thousands)

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

Other information. In addition to the basic financial statements and the accompanying notes, this report also presents certain required supplementary information on the City's General Fund budget, which is adopted on an annual basis, and schedules of funding progress related to pension and retirement plans. A budgetary comparison statement has been provided for this fund in order to demonstrate budgetary compliance with this budget.

Government-wide Financial Analysis

GASB Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*, requires that the City provide a comparative analysis of government-wide data. Below is a comparative summary of the governmental activities and business-type activities as required by GASB Statement No. 34:

City of San Antonio, Texas Net Assets Year Ended September 30, 2005 (With Comparative Totals for September 30, 2004)						
	Governmental Activities		Business-Type Activities		Total Primary Government	
	2005	2004	2005	2004	2005	2004
Current and other assets	\$ 990,155	\$ 708,633	\$ 236,980	\$ 202,559	\$ 1,227,135	\$ 911,192
Capital assets	3,068,559	3,047,629	307,740	296,394	3,376,299	3,344,023
Total assets	4,058,714	3,756,262	544,720	498,953	4,603,434	4,255,215
Current and other liabilities	168,847	135,687	30,074	11,900	198,921	147,587
Long-term liabilities	1,613,274	1,312,631	273,576	259,433	1,886,850	1,572,064
Total liabilities	1,782,121	1,448,318	303,650	271,333	2,085,771	1,719,651
Net assets:						
Investment in capital assets, net of related debt	2,042,288	2,118,418	212,715	197,929	2,255,003	2,316,347
Restricted	101,253	89,867	26,636	23,720	127,889	113,587
Unrestricted	133,052	99,659	1,719	5,971	134,771	105,630
Total net assets	\$ 2,276,593	\$ 2,307,944	\$ 241,070	\$ 227,620	\$ 2,517,663	\$ 2,535,564

For the year ended September 30, 2005, total assets exceeded liabilities by \$2,517,663. The largest portion of the City's net assets, \$2,255,003 (89.6%) represents its investment in capital assets less any related debt used to acquire those assets that are still outstanding, and includes assets such as land, infrastructure, improvements, buildings, machinery and equipment.

Capital assets are used to provide services to the citizens of San Antonio and are not available for further spending. Although the City's investment in capital assets is reported net of related debt, the resources needed to repay the debt must be provided from other sources, as capital assets cannot be used to liquidate these liabilities.

Of the total net assets, \$127,889 (5.1%) represents resources that are subject to external restrictions on how they may be used. The remaining \$134,771 (5.3%) represents unrestricted net assets, which can be used to meet the government's ongoing obligations to citizens and creditors.

(amounts are expressed in thousands)

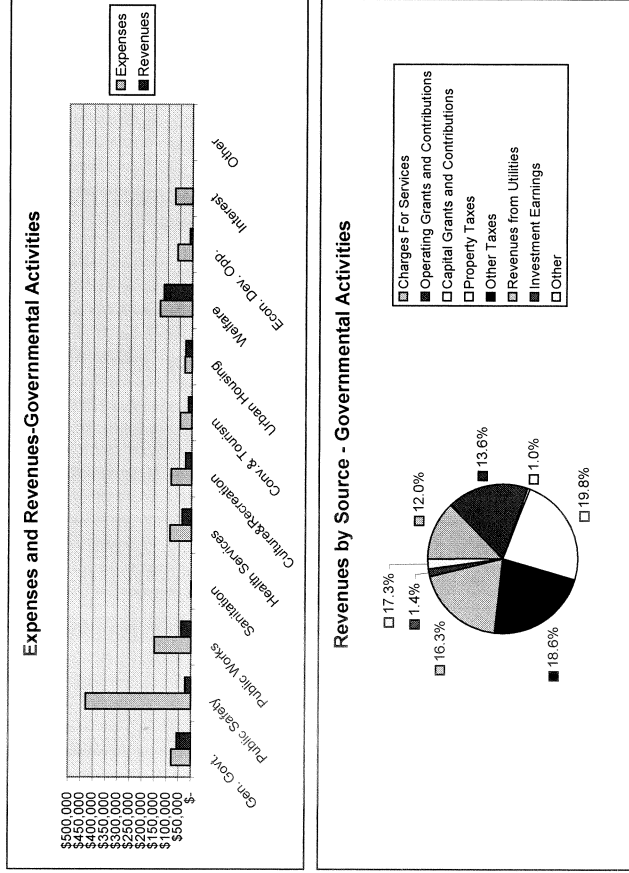
City of San Antonio, Texas Changes in Net Assets Year ended September 30, 2005 (With Comparative Totals for September 30, 2004)						
	Governmental Activities		Business-Type Activities		Total Primary Government	
	2005	2004	2005	2004	2005	2004
Revenues:						
Program revenues:						
Charges for services	\$ 147,109	\$ 133,709	\$ 107,869	\$ 103,739	\$ 254,978	\$ 237,448
Operating grants and contributions	198,185	168,120			198,185	168,120
Capital grants and contributions	8,256	16,614	2,223	27	10,479	16,641
General revenues:						
Property taxes	269,138	257,514			269,138	257,514
Other taxes	253,239	238,700			253,239	238,700
Revenues from utilities	222,162	196,793			222,162	196,793
Investment earnings	19,931	7,189	5,434	2,046	25,365	9,235
Miscellaneous	22,431	28,542	9,962	10,378	32,393	38,920
Gain on sale of capital assets	1,507	611	96		1,603	611
Capital contributions		1,585				1,585
Total revenues	\$ 1,141,958	\$ 1,049,377	\$ 125,584	\$ 116,190	\$ 1,267,542	\$ 1,165,567
Expenses:						
Primary government:						
Governmental activities:						
General government	80,018	63,610			80,018	63,610
Public safety	428,382	428,607			428,382	428,607
Public works	149,476	116,629			149,476	116,629
Sanitation	2,731	2,787			2,731	2,787
Health services	89,011	82,233			89,011	82,233
Environmental protection and control		36				36
Culture and recreation	84,555	80,051			84,555	80,051
Convention and tourism	48,364	50,100			48,364	50,100
Conservation	2				2	
Urban redevelopment and housing	29,764	23,981			29,764	23,981
Welfare	131,840	116,701			131,840	116,701
Economic development opportunity	60,461	21,277			60,461	21,277
Interest on long-term debt	70,655	55,855			70,655	55,855
Business-type activities:						
Airport			46,868	49,427	46,868	49,427
Parking facilities			8,413	6,264	8,413	6,264
Environmental services			54,703	51,227	54,703	51,227
Total expenses	1,175,459	1,041,867	109,984	106,918	1,285,443	1,148,785
Increase (decrease) in net assets before transfers	(33,501)	7,510	15,600	9,272	(17,901)	16,782
Transfers	2,150	2,443	(2,150)	(2,443)		
Net increase in net assets	(31,351)	9,953	13,450	6,829	(17,901)	16,782
Beginning, net assets	2,307,944	2,297,991	227,620	220,791	2,535,564	2,518,782
Ending, net assets	\$ 2,276,593	\$ 2,307,944	\$ 241,070	\$ 227,620	\$ 2,517,663	\$ 2,535,564

(amounts are expressed in thousands)

Governmental Activities

The City's total revenues were \$1,267,542 for fiscal year ended September 30, 2005. Revenues from governmental activities totaled \$1,141,958 and revenues from business-type activities totaled \$125,584. General revenues represented 63.4% of the City's total revenue, while program revenues provided 36.6% of revenue received in fiscal year 2005.

Expenses for the City totaled \$1,285,443. Governmental activity expenses totaled \$1,175,459, or 91.4% of total expenses.



Governmental Activities decreased the City's net assets by \$31,351. The reason for the change is as follows:

- Revenues from utilities increased by \$25,369 because of rate increases and because of an unusually hot and dry year.
- General Government expenses increased by \$16,408 because of budgeted increases in salaries and benefits and increases in other expenditures.
- Interest on Long Term Debt increased \$14,800 because of increased bond activity.
- The increase of Public Work expenses was primarily attributed to a \$7,261 increase for street maintenance and improvement projects and \$12,694 was related to expenses incurred for Hurricane Katrina.
- Expenditures for Economic Development increased by \$39,184 was related to construction costs of the Convention Center Hotel Project

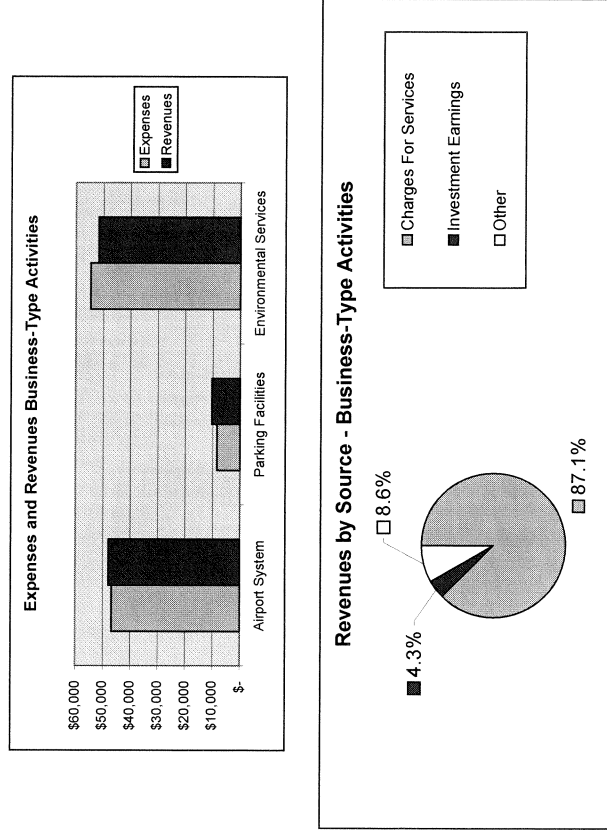
(amounts are expressed in thousands)

Business-Type Activities/Proprietary Funds

Program revenues for the City's business-type activities totaled \$107,869, which is \$4,130 higher than the previous fiscal year. Expenses for business-type activities were \$109,984 compared to prior year's expenses of \$106,918. The current year's increase in expenses is attributed to increased expenses incurred in the Parking and Environmental Services funds over the prior year. The remaining revenue was a result of interest and other miscellaneous items.

Business-Type Activities increased the City's net assets by \$13,450 primarily because of the following:

- Charges for Services increased \$4,130 because of an increase in customers served as well as various fee increases implemented in FY 2005.
- Investment earnings increased by \$3,388 when compared to FY 2004.
- A \$2,196 increase in Capital Grant Contributions in the Airport System Fund.



Financial Analysis of Governmental Funds

Activities of the Primary Government's General Fund, Special Revenue Funds, Debt Service Funds, and Convention Center Hotel Finance Corporation are considered general government functions. The General Fund is the City's general operating fund. Special Revenue Funds are used to account for the proceeds of specific revenue sources that are legally restricted as to expenditure. The Debt Service Funds are used to account for financial activity related to the City's general bonded indebtedness, as well as other long-term obligations. The Convention Center Hotel Finance Corporation Fund, established in 2005, is used to account for finance and costs associated with the design, development, and construction of the Hotel Project.

(amounts are expressed in thousands)

Revenues from taxes increased by \$26,163 which is primarily attributable to: (1) a \$11,624 or 4.5% increase in property tax revenue in the General Fund, (2) a \$14,294 or 9.6% increase in sales tax revenue in the General Fund, and (3) a \$4,867 or 4.9% increase in property tax revenue for the Debt Service Fund as a result of increased property valuation, new construction, and annexation. Revenues for the utilities category, which is represented in the City's General Fund increased by \$25,369 or 12.9%. This is primarily attributed to an increase of \$23,878 in the City's payment from CPS, which is based on CPS' gross revenues. CPS revenues are impacted by a number of variables such as fuel costs, weather, types of electric generation used as well as other factors. In this first year of operation, the Convention Center Hotel Finance Corporation received revenues from the sale of revenue bonds in the amount of \$208,145 and interest of \$2,022.

The total fund balance of the General Fund at year-end was \$118,413, an increase of \$19,903 from the total fund balance of \$98,510 for the close of fiscal year 2004. The total unreserved general fund balance for fiscal year 2005 is \$107,491, which represents \$31,950 in designated and \$75,540 in undesignated fund balance. The undesignated fund balance, which represents amounts available for additional appropriations, in the General Fund at the close of the fiscal year increased by \$14,305 from the previous year.

The total fund balance of the Debt Service Fund at year-end was \$85,127; an increase of \$1,405 from the total fund balance for the close of fiscal year 2004. The entire fund balance is reserved for payment of debt service.

The Convention Center Hotel Finance Corporation has a total fund balance of \$173,286, which is available for the payment of costs associated with the design, development, and construction of the Convention Center Hotel Project.

General Fund Budgetary Highlights

Significant Variances in Budget Appropriations (Budgetary Basis)			
General Fund			
	Original Budget	Final Budget	Actual Results
General Government	\$ 79,513	\$ 87,406	\$ 66,747
Public Safety	400,696	405,154	404,491
Public Works	10,698	10,698	10,478
Health Services	13,948	14,245	14,379
Sanitation	2,886	2,886	2,583
Welfare	20,837	22,019	21,578
Culture and Recreation	66,032	66,727	63,479
Economic Development			
and Opportunity	4,054	4,525	4,553
Transfers to Other Funds	75,210	87,057	86,649
Total	\$ 673,874	\$ 700,717	\$ 674,937

(amounts are expressed in thousands)

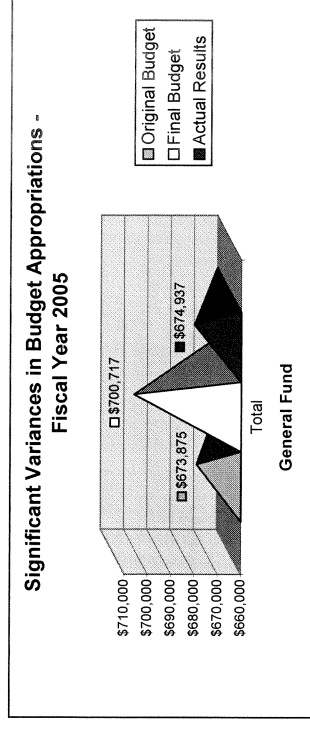
Changes in original budget appropriations to the final amended budget appropriations were a \$26,843 increase in appropriations. This increase can be summarized by the following discussion.

- General Government has a \$7,893 increase composed of \$8,247 of budget carry forwards and a \$354 budget decrease. Of the \$8,247 of budget carry forwards, \$5,079 is for Special Projects and \$2,007 is non-departmental carry forwards. The \$354 budget decrease is made up of decreases in special projects and non-departmental of \$2,635 and \$324, respectively, offset by budget increases in various departments of \$2,607.
- Of the \$4,458 increase in Public Safety, \$2,227 is due to budget carry forwards and \$2,231 of budget increases. Major increases to budget carry forwards include \$1,276 within the Police Department and \$462 for the Fire Department. The \$2,231 budget increase is attributable to increases to the Police and Fire Departments of \$618 and \$1,569 respectively.
- Health Services had a \$297 budget increase, which consists of \$26 of budget carry forwards and \$271 of budget increases.
- All of the \$1,182 increase in Welfare is due to a budget increase.
- Culture and Recreation's \$695 increase is due to a \$1,340 increase for budget carry forwards and \$645 as a decrease in budget. The increase in budget carry forwards is due to increases in the Library and Parks and Recreation departments of \$851 and \$489, respectively. The \$645 decrease in budget is within the Parks and Recreation department.
- The \$471 increase in Economic Development and Opportunity is due to a \$294 increase in budget carry forwards and a \$177 budget increase.
- The \$11,847 increase in transfers is due to amounts funded from various government functions.

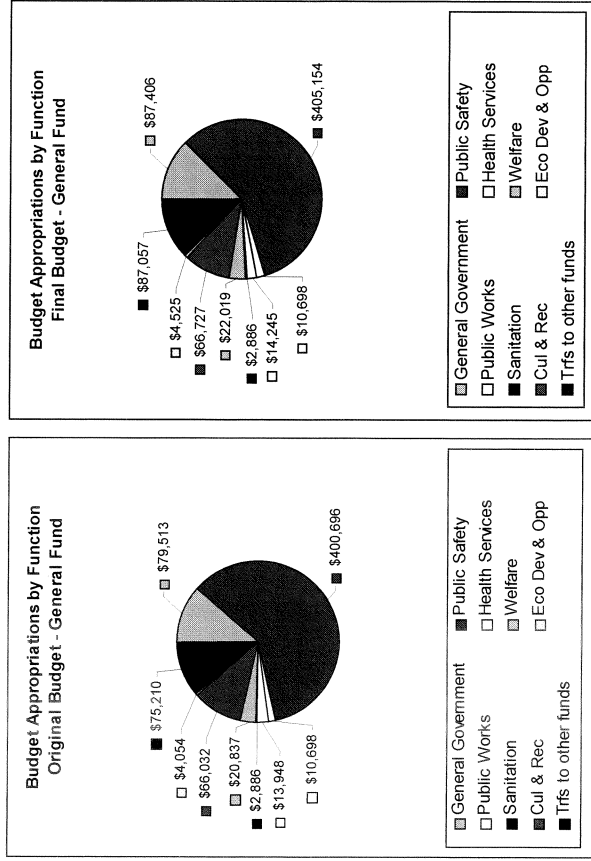
Final budgeted appropriations for the General Fund were \$700,717 while actual expenditures were \$674,937, creating a positive variance of \$25,780. Significant variances are as follows:

- General Government had a \$20,659 positive variance, which is composed of \$11,819 of budgeted personnel expenditures, \$1,226 of improvements to computers to include software licenses, \$5,582 in various contractual services, and \$1,888 in unrealized expenditures for commodities such as supplies, repair and maintenance, and \$34 in unrealized capital expenditures.
- Culture and Recreation had a positive variance of \$3,248, which is due to a negative variance of (\$1,921) of budgeted salaries, \$4,751 in contractual services, \$657 in expenditures for commodities, \$112 in other expenses and negative variance of (\$351) in capital expenditures.

The following charts provide a comparison of the City's budget appropriations.



(amounts are expressed in thousands)



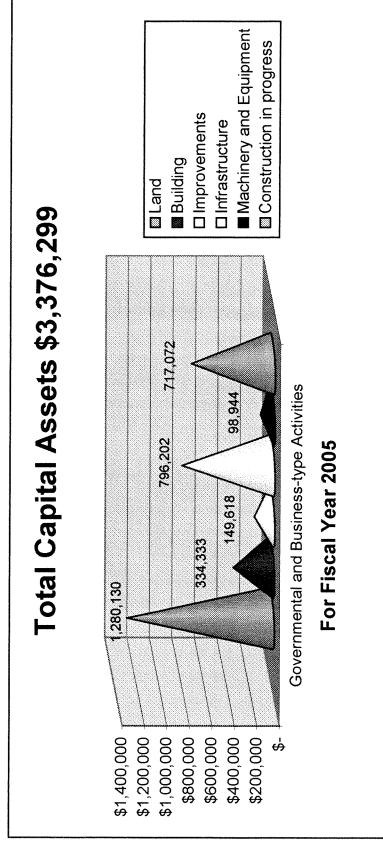
Capital Assets

The City of San Antonio's investment in capital assets for its governmental and business-type activities as of September 30, 2005, amounts to \$3,376,299 (net of accumulated depreciation). This investment in capital assets includes land, buildings, improvements, infrastructure, and machinery and equipment. The total increase in the City's investment in capital assets for the current fiscal year was 0.9%, which is comprised of a 0.7% increase for governmental activities and a 3.9% increase for business-type activities.

	Governmental Activities		Business-Type Activities		Total	
	2005	2004	2005	2004	2005	2004
Land	\$ 1,268,142	\$ 1,259,362	\$ 11,988	\$ 11,988	\$ 1,280,130	\$ 1,271,350
Buildings	228,284	220,650	106,049	72,140	334,333	292,790
Improvements	65,579	40,379	84,039	88,052	149,618	128,431
Infrastructure	796,202	788,894			796,202	788,894
Machinery and Equipment	95,589	92,823	3,355	3,594	98,944	96,417
Construction in Progress	614,763	645,521	102,309	120,620	717,072	766,141
Totals	\$ 3,068,559	\$ 3,047,629	\$ 307,740	\$ 296,394	\$ 3,376,299	\$ 3,344,023

(amounts are expressed in thousands)

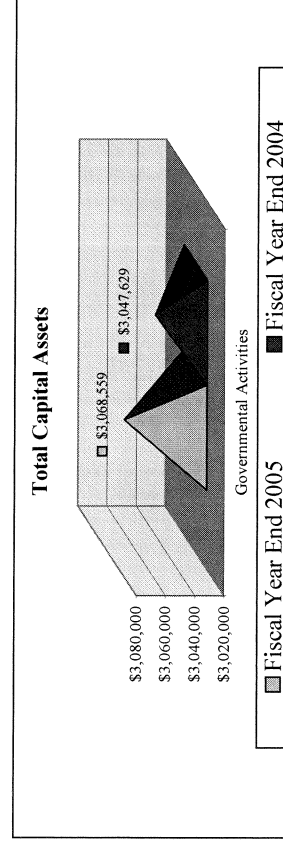
The following schedule provides a summary of the City's capital assets:



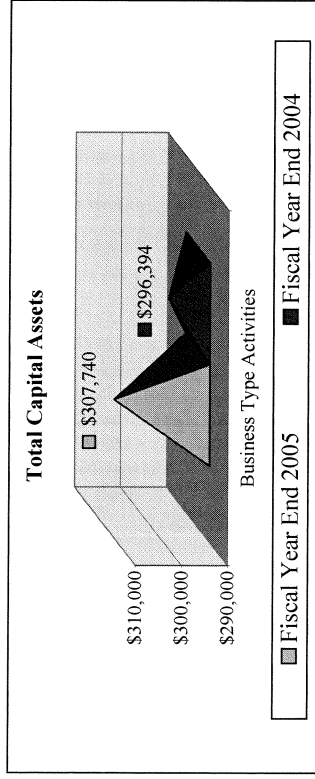
Change in Capital Assets September 30, 2005

	Governmental Activities	Business-Type Activities	Total
Beginning Balance	\$ 3,047,629	\$ 296,394	\$ 3,344,023
Additions	119,455	60,178	179,633
Deletions	(9,441)	(39,018)	(48,459)
Accumulated Depreciation	(89,084)	(9,814)	(98,898)
Ending Balance	\$ 3,068,559	\$ 307,740	\$ 3,376,299

The following charts provide a summary of the changes in capital assets:



(amounts are expressed in thousands)



Additional information on the City's capital assets can be found in Note 4 of the notes to the financial statements.

Debt Administration

Long-term Debt

At the end of the current fiscal year, the City of San Antonio had a total of \$1,700,342 in bonds, certificates, and revenue bonds, an increase of 21.9% over last year. Additional information on the City of San Antonio's long-term debt, including descriptions of the new issues, can be found in Note 6 in the Notes to the Financial Statements.

City of San Antonio's Outstanding Debt September 30, 2005 and 2004			
Governmental Activities		2004	
Bonds Payable:			
General Obligation Bonds	\$ 658,450	\$ 655,141	
Tax-Exempt Certificate of Obligation	194,675	214,470	
Taxable Certificates of Obligation	6,850	4,580	
Revenue Bonds	556,152	264,697	
Total	\$ 1,416,127	\$ 1,138,888	
Business-Type Activities		2004	
Bonds Payable:			
General Obligation Bonds	\$ 12,115	\$ 13,245	
Revenue Bonds	272,100	242,855	
Total	\$ 284,215	\$ 256,100	

(amounts are expressed in thousands)

On September 30, 2005, outstanding bonds and certificates debt totaled \$1,416,127. In 2005, the City issued additional indebtedness for a total of \$129,605. The \$129,605 is comprised of \$13,435 in certificates of obligation and \$116,170 in general obligation bonds. The general obligation bonds will be utilized to refund a portion of the City's outstanding tax-supported debt, fund capital improvements to include streets and pedestrian improvements; drainage improvements; park and recreation facilities improvements; library improvements; public health and safety improvements. In April 2005, the City issued \$10,535 in tax-exempt certificates of obligation bonds that will be utilized to fund capital improvements to include public safety, consisting of constructing, renovating, and improving existing fire stations; street, sidewalk, bridge, and drainage improvements; improvements and renovations to existing municipal facilities; acquiring, constructing, renovating the City's park facilities; constructing improvements for flood control, dams, landscaping, amenities along the San Antonio River; the purchase of materials, supplies, machinery, land, and rights-of-way for authorized needs and purposes relating to public safety, drainage, street, parks, and public works purposes; and professional services related to the construction and financing of the aforementioned projects. In May 2005, the City issued \$2,900 in taxable certificates of obligations, which were used to fund improvement projects to the Alamodome. Also, in April 2005, the City issued \$61,060 of Municipal Drainage Utility System Revenue Bonds, Series 2005. Proceeds of the 2005 Municipal Drainage Utility System Revenue Bonds will be used to finance the costs of drainage improvements, including the acquisition, construction, and repair of structures, equipment, and facilities for the City's Municipal Drainage Utility System. The City issued the following: \$129,930 Contract Revenue Empowerment Zone Bonds, Series 2005A and \$78,215 Contract Revenue Bonds, Series 2005B for Texas Convention Center Hotel Finance Corporation. Hotel Investments, L.P. will be loaned the proceeds from the Series 2005 bonds by the Texas Convention Center Hotel Finance Corporation. Hotel Investments, L.P. will use the proceeds of the Series 2005 Bonds to finance a portion of the costs to design, develop, construct, equip, furnish, and open a full-service hotel.

Standard & Poor's, Moody's and Fitch's underlying rating for City obligations are as follows:

General Obligation/ Certificates of Obligation	Standard & Poor's	Moody's	Fitch
	AA+	Aa2	AA+
Airport	A+	A1	A+
Airport PFC	A-	A2	A+
Convention Center - Prior Lien	A+	A1	A+
Convention Center - Subordinate Lien	A+	A2	A
Parking	A+	A2	A+
Drainage	AA-	A1	A+

The Constitution of the State of Texas and the City Charter limit the amount of debt the City may incur. The City Charter establishes a limitation on the general obligation debt supported by ad valorem taxes to an amount not to exceed 10% of the total assessed valuation. The total assessed valuation for the fiscal year ending 2005 was \$51,824,208, which provides a debt ceiling of \$5,182,421.

Requests for Information

This financial report is designed to provide a general overview of the City's position for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Finance Department, P.O. Box 839966, San Antonio, TX 78283-3966.

(amounts are expressed in thousands)



City of San Antonio Texas

Basic Financial Statements

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CITY OF SAN ANTONIO, TEXAS

STATEMENT OF NET ASSETS
AS OF SEPTEMBER 30, 2005
(In Thousands)

	PRIMARY GOVERNMENT			COMPONENT UNITS
	GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTAL	
Assets				
Cash and Cash Equivalents	\$ 242,753	\$ 1,450	\$ 244,203	\$ 67,158
Investments	531,510	14,647	546,157	310,854
Receivables, net	125,559	6,771	132,330	213,500
Due from Fiduciary Funds	700		700	
Due from Other Governmental Agencies, net	55,397	(4,392)	55,397	3,530
Internal Balances	4,392			
Materials and Supplies, at Cost	5,948	718	6,666	119,859
Prepaid Expenses	731	17	748	34,501
Deposits	542		542	
Restricted Assets:				
Cash and Cash Equivalents		22,622	22,622	141,614
Investments		189,072	189,072	1,244,247
Receivables - Accrued Interest		1,315	1,315	7,591
Capital Assets:				
Non-depreciable	1,882,905	114,297	1,997,202	868,665
Depreciable, net	1,185,654	193,443	1,379,097	6,167,103
Assets Held for Resale				8,210
Prepaid Rent Long-Term - Leaseback				516,182
Unamortized Debt Expense	22,623	4,760	27,383	37,661
Total Assets	4,058,714	544,720	4,603,434	9,740,675
Liabilities				
Accounts Payable and Other Current Liabilities	131,558	12,407	143,965	228,412
Unearned Revenues	20,178	596	20,774	1,897
Accrued Interest	11,960	1	11,961	
Liabilities Payable from Restricted Assets		13,465	13,465	19,294
Accrued Bond and Certificate Interest		3,605	3,605	150,911
Due To:				
Other Governmental Agencies	5,151		5,151	1,108
Noncurrent Liabilities:				
Due Within One Year	108,862	334	109,196	1,416,157
Due in More Than One Year	1,504,412	273,242	1,777,654	3,767,143
Total Liabilities	1,782,121	303,650	2,085,771	5,584,922
Net Assets				
Invested in Capital Assets,				
Net of Related Debt	2,042,288	212,715	2,255,003	2,976,175
Restricted for:				
Debt Service	88,219	26,636	114,855	17,254
Capital Projects				579,546
Equipment Renewal and Replacement				175,396
Perpetual Care:				
Expendable	10,209		10,209	
Nonexpendable	2,825		2,825	
Unrestricted	133,052	1,719	134,771	407,382
Total Net Assets	\$ 2,276,593	\$ 241,070	\$ 2,517,663	\$ 4,155,753

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The accompanying notes are an integral part of these basic financial statements.

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FUNCTION/PROGRAM ACTIVITIES	EXPENSES	CHARGES FOR SERVICES	PROGRAM REVENUES OPERATING GRANTS AND CONTRIBUTIONS	CAPITAL GRANTS AND CONTRIBUTIONS
Primary Government				
Governmental Activities:				
General Government	\$ 80,018	\$ 57,660	\$ -	\$ -
Public Safety	428,582	7,861	12,535	3,130
Public Works	149,476	34,201	3,421	3,862
Sanitation	2,731	-	193	7
Health Services	89,011	10,252	27,459	76
Culture and Recreation	84,555	19,583	4,588	965
Convention and Tourism	48,364	14,740	-	-
Conservation	2	-	2	-
Urban Redevelopment and Housing	29,764	-	26,761	7
Welfare	131,840	327	114,822	209
Economic Development Opportunity	60,461	-	8,404	-
Interest on Long-Term Debt	70,655	2,485	-	-
Total Governmental Activities	1,175,459	141,109	198,185	8,256
Business-Type Activities:				
Airport System	46,868	45,791	-	-
Parking Facilities	8,413	10,325	-	2,223
Environmental Services	54,703	51,753	-	-
Total Business-Type Activities	109,984	107,869	-	2,223
Total Primary Government	1,285,443	254,978	198,185	10,479
Component Units:				
San Antonio Water System	265,029	262,687	-	59,742
City Public Service	1,465,609	1,422,405	-	47,666
Other Component Units	53,747	14,039	-	38,409
Total Component Units	1,784,376	1,699,131	-	145,817
General Revenues:				
Taxes:				
Property Taxes				
General Sales and Use Taxes				
Selective Sales and Use Taxes				
Gross Receipts Business Taxes				
Occupancy Taxes				
Penalties and Interest on Delinquent Taxes				
Revenues from Utilities				
Investment Earnings				
Miscellaneous				
Gain on Sale of Capital Assets				
Transfers (Net)				
Total General Revenues, Special Items, and Transfers				
Change in Net Assets				
Net Assets, Beginning				
Prior Period Adjustment				
Net Assets, Ending				

**BALANCE SHEET
GOVERNMENTAL FUNDS
AS OF SEPTEMBER 30, 2005**
(In Thousands)

	MAJOR FUNDS				CONVENTION CENTER	TOTAL GOVERNMENTAL FUNDS	
	GENERAL	DEBT SERVICE	FINANCE CORPORATION	NONMAJOR GOVERNMENTAL FUNDS			
Assets							
Cash and Cash Equivalents	\$ 1,928	\$ 21,946	\$ 177,355	\$ 36,817	\$	238,046	
Investments	26,057	60,080		395,030		481,167	
Receivables	103,948	9,416	466	50,683		164,513	
Allowance for Uncollectibles	(19,827)	(937)		(19,991)		(40,755)	
Prepaid Expenditures	2					2	
Due from Other Funds	44,687	1,539		22,149		68,375	
Due from Other Governmental Agencies	83			54,781		54,864	
Materials and Supplies, at Cost	2,712			1,190		3,902	
Deposits				261		261	
Total Assets	\$ 159,590	\$ 92,044	\$ 177,821	\$ 540,837		\$ 970,292	
Liabilities and Fund Balances							
Liabilities:							
Vouchers Payable	\$ 4,000	\$ -	\$ 4,535	\$ 4,901	\$	13,436	
Accounts Payable - Other	4,620			41,466		46,086	
Accrued Payroll	8,974			5,095		14,030	
Accrued Leave Payable	5,031			1,261		6,292	
Unearned Revenues	16,888	6,917		19,073		42,878	
Due To:							
Other Funds	1,664			68,512		70,176	
Other Governmental Agencies				4,440		4,440	
Total Liabilities	\$ 41,177	\$ 6,917	\$ 4,535	\$ 144,709		\$ 197,338	
Fund Balances:							
Reserved:							
Reserved for Encumbrances	8,709		3,598	99,067		110,974	
Reserved for Materials and Supplies, at Cost	2,712			833		3,565	
Reserved for Prepaid Expenditures	2					2	
Reserved for Debt Service		85,127				85,127	
Unreserved:							
Designated:							
Designated: Special Revenue Funds	31,950			6,085		31,950	
Designated: Permanent Funds				2,825		6,085	
Undesignated:							
Undesignated: Special Revenue Funds	75,540			85,644		75,540	
Undesignated: Capital Projects Funds			169,588	191,532		85,644	
Undesignated: Permanent Funds				10,122		361,120	
Total Fund Balances	\$ 118,413	\$ 85,127	\$ 173,286	\$ 396,128		\$ 772,954	
Total Liabilities and Fund Balances	\$ 159,590	\$ 92,044	\$ 177,821	\$ 540,837		\$ 970,292	

**RECONCILIATION OF THE BALANCE SHEET
TO THE STATEMENT OF NET ASSETS
GOVERNMENTAL ACTIVITIES
AS OF SEPTEMBER 30, 2005**
(In Thousands)

Amounts reported for governmental activities in the Statement of Net Assets are different because:

Fund Balances - Total Governmental Funds

\$ 772,954

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the governmental funds.

Governmental capital assets:

Land and Land Improvements	1,268,142
Construction In Progress	614,763
Buildings	396,373
Improvements	106,838
Infrastructure Assets	2,054,838
Machinery and Equipment	96,481
Less: Accumulated Depreciation	(1,514,558)
Total Capital Assets	3,022,877

Some of the City's revenues will be collected after year-end but are not available soon enough to pay for the current periods expenditures and, therefore, are not reported in the governmental funds (See Footnote 14).

23,958

Internal service funds are used by management to change the cost of certain activities to individual funds. The assets and liabilities of the internal service funds are reported with governmental activities in the Statement of Net Assets.

50,741

Long-term liabilities, including bonds payable, are not due and payable in the current period and, therefore, are not reported in the governmental funds (See Footnote 14).

Governmental Bonds Payable	(1,438,372)
Premium on Bonds	(49,799)
Deferred Amount on Refunding	13,839
Leases Payable	(6,079)
Amounts received from notes & loans	(1,369)
Unamortized Debt Expense	22,623
Accrued Interest	(11,960)
Arbitrage Rebate	(1,688)
Compensated Absences	(121,132)

(1,593,937)

Net assets of Governmental Activities

\$ 2,276,593

The accompanying notes are an integral part of these basic financial statements.

The accompanying notes are an integral part of these basic financial statements.

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
YEAR ENDED SEPTEMBER 30, 2005
(In Thousands)

	MAJOR FUNDS			CONVENTION CENTER HOTEL FINANCE CORPORATION	NONMAJOR GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
	GENERAL	DEBT SERVICE				
Revenues						
Taxes:						
Property Taxes	\$ 171,229	\$ 98,923	\$ -	\$ -	\$ 1,338	\$ 271,490
General Sales and Use Taxes	162,786				4,546	167,332
Selective Sales and Use Taxes	4,473					4,473
Gross Receipts Business Taxes	26,274					26,274
Occupancy Taxes					51,717	51,717
Penalties and Interest on Delinquent Taxes		1,137			3,434	4,571
Licenses and Permits	2,268				29	2,297
Intergovernmental	20,716					20,716
Revenues from Utilities	3,055				187,196	190,251
Charges for Services	221,775					221,775
Fines and Forfeits	33,622				73,642	107,264
Miscellaneous	12,025					12,025
Investment Earnings	11,841		16		14,991	26,848
In-Kind Contributions	2,445	3,970	2,022		10,107	18,544
Total Revenues	672,509	104,030	2,038		24,872	1,147,015

Expenditures						
Current:						
General Government	64,020				5,312	69,332
Public Safety	402,544				17,090	419,634
Public Works	10,478				75,462	85,940
Health Services	13,995				74,538	88,533
Sanitation	2,576				192	2,768
Welfare	19,757				111,255	131,012
Culture and Recreation	63,010				16,576	79,586
Convention and Tourism					48,315	48,315
Conservation					2	2
Urban Redevelopment and Housing					25,557	25,557
Economic Development and Opportunity	4,392			36,963	11,945	16,337
Capital Projects					109,887	146,850
Debt Service:						
Principal Retirement		57,581			57,581	57,581
Interest		60,202			60,202	60,202
Insurance Costs		1,027			1,027	1,027
Total Expenditures	580,772	118,810		36,963	496,131	1,232,676

Excess (Deficiency) of Revenues Over (Under) Expenditures	91,737	(14,780)		(34,925)	(127,693)	(85,661)
Other Financing Sources (Uses)						
Long-Term Debt Issued		86,010			106,319	192,329
Payments to Refunded Bond Escrow Agent		(93,163)			(93,163)	(93,163)
Amounts from Notes and Loans			208,145		2,462	210,607
Premium on Long-term Debt		6,914	66		5,924	12,904
Transfers In	14,122	16,423			129,776	159,821
Transfers Out	(85,956)				(74,455)	(160,611)
Total Other Financing Sources (Uses)	(71,834)	16,184		208,211	169,226	321,887
Net Change in Fund Balances	19,903	1,404		173,286	41,633	236,226
Fund Balances, October 1	98,510	83,723			354,495	536,728
Fund Balances, September 30	\$ 118,413	\$ 85,127	\$	\$ 173,286	\$ 396,128	\$ 772,954

The accompanying notes are an integral part of these basic financial statements.

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES
YEAR ENDED SEPTEMBER 30, 2005
(In Thousands)

Amounts reported for governmental activities in the Statement of Activities are different because:

Net change in Fund Balances - Total Governmental Funds \$ 236,226

Governmental funds report capital outlays as expenditures. However, in the Statement of Activities, the cost of those assets is depreciated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays exceed depreciation in the current period.

Donated capital assets	364
Expenditures for Capital Assets	99,821
Less Current Year Deletions	(201)
Less Current Year Depreciation	(84,483)

15,501

Revenues in the Statement of Activities that do not provide current financial resources are not reported as revenues in the funds.

(11,194)

Bond proceeds provide current financial resources to governmental funds, but issuing debt increases long-term liabilities in the Statement of Net Assets. Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long term liabilities in the Statement of Net Assets. This is the amount by which proceeds exceeded repayments (See Footnote 14).

Bond and Loan Amounts	(440,525)
Payments to Escrow Agent	93,163
Amortization of Bond Premiums and Deferred Charges (Net)	14,721
Principal Payments	57,581

(275,060)

Some expenses reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds (See Footnote 14).

(9,990)

Internal service funds are used by management to charge the cost of certain activities to individual funds. The net (expense) of the internal service funds is reported with governmental activities.

13,166

Change in Net Assets of Governmental Activities

\$ (31,351)

The accompanying notes are an integral part of these basic financial statements.

— CITY OF SAN ANTONIO, TEXAS —
STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
AS OF SEPTEMBER 30, 2005
(In Thousands)

	BUSINESS-TYPE ACTIVITIES ENTERPRISE FUNDS				GOVERNMENTAL ACTIVITIES
	AIRPORT SYSTEM	PARKING FACILITIES	NONMAJOR ENTERPRISE FUND-ENVIRONMENTAL SERVICES	TOTAL	
ASSETS					
Current Assets:					
Cash and Cash Equivalents	\$ 968	\$ 213	\$ 269	\$ 1,450	\$ 4,707
Investments	12,170	1,749	728	14,647	50,343
Receivables					
Other Accounts	2,018	114	17	2,149	967
Less: Allowance for Uncollectibles	(440)			(440)	(125)
Accrued Interest	75	20	19	114	391
Accrued Revenue	788		4,160	4,948	3
Due From Other Funds	543	2,724	10	3,277	13,630
Due From Other Governmental Agencies					759
Materials and Supplies, at Cost	500	209	9	718	(143)
Prepaid Expenses	17			17	2,046
Deposits					729
Total Current Assets	16,639	5,029	5,212	26,880	73,588
Noncurrent Assets:					
Restricted Assets:					
Debt Service Accounts:					
Cash and Cash Equivalents	9,184	2,849		12,033	
Investments	17,477	5,421		22,898	
Receivables-Accrued Interest	68	15		83	
Due From Other Funds		4,843		4,843	
Construction Accounts:					
Cash and Cash Equivalents	7,622	151	18	7,791	
Investments	122,181	1,653	269	124,103	
Receivables-Accrued Interest	713	50	23	786	
Due From Other Funds	2,224	6,033		8,259	
Improvement and Contingency Accounts:					
Cash and Cash Equivalents	2,272	93	5	2,370	
Investments	34,165	1,398	81	35,644	
Receivables-Accrued Interest	376	9	3	388	
Due From Other Funds			409	409	
Other Restricted Accounts:					
Cash and Cash Equivalents	323	105		428	
Investments	4,851	1,576		6,427	
Receivables-Accrued Interest	47	11		58	
Due From Other Funds	4,938			4,938	
Total Restricted Assets	206,441	24,211	808	231,460	
Capital Assets:					
Land	2,970	8,125	893	11,988	
Buildings	144,248	29,192	46	173,486	464
Improvements Other Than Buildings	156,110	1,283	3,025	160,418	195
Machinery and Equipment	10,866	579	3,840	15,285	119,580
Construction in Progress	98,382		598	102,309	
Total Capital Assets	412,576	42,508	8,402	463,486	120,239
Less: Accumulated Depreciation	142,056	10,236	3,454	155,746	74,557
Net Capital Assets	270,520	32,272	4,948	307,740	45,682
Unamortized Debt Expense	4,017	743		4,760	
Total Noncurrent Assets	480,978	57,226	5,756	543,960	45,682
Total Assets	\$ 497,617	\$ 62,255	\$ 10,968	\$ 570,840	\$ 119,270

— CITY OF SAN ANTONIO, TEXAS —
STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
AS OF SEPTEMBER 30, 2005
(In Thousands)

	BUSINESS-TYPE ACTIVITIES ENTERPRISE FUNDS				GOVERNMENTAL ACTIVITIES
	AIRPORT SYSTEM	PARKING FACILITIES	NONMAJOR ENTERPRISE FUND-ENVIRONMENTAL SERVICES	TOTAL	
LIABILITIES					
Current Liabilities:					
Vouchers Payable	\$ 397	\$ 59	\$ 1,169	\$ 1,625	\$ 3,966
Accounts Payable-Other	6,439	111	2,142	8,692	52,996
Accrued Payroll	187	109	646	1,242	1,044
Accrued Leave Payable	174	16	144	334	616
Unearned Revenues	596		1	596	693
Accrued Interest					355
Lease Purchase Agreement		6,895	409	7,304	13,277
Due to Other Funds					
Total Current Liabilities Payable from Current Assets	8,093	7,190	4,511	19,794	72,947
Restricted Assets:					
Vouchers Payable	484	362	2	848	
Accrued Bond and Certificate Interest	3,311	294		3,605	
Current Portion of Bonds and Certificates	9,615	1,930		11,545	
Due to Other Funds	5,477	6,799	148	12,276	96
Lease Purchase			200	148	
Other Payables	1,565	7		1,772	
Total Current Liabilities Payable from Restricted Assets	20,452	9,392	350	30,194	96
Total Current Liabilities	28,545	16,582	4,861	49,988	73,043
Noncurrent Liabilities:					
Revenue Bonds (Net of Current Portion)	238,490	23,395		261,885	
General Obligation Bonds and Certificates (Net of Current Portion)		10,785		10,785	
Unamortized Premium/Discount on new Series	3,773	(761)		3,012	
Less: Deferred Amount on Refunding	(3,502)	(1,551)		(3,053)	
Accrued Leave Payable	868	82	718	1,668	613
Lease Purchase			115	115	702
Due to Other Governmental Agencies					711
Other Payables			830	830	
Total Noncurrent Liabilities	239,629	31,980	1,663	272,242	2,026
Total Liabilities	288,174	48,532	6,524	323,230	75,069
NET ASSETS					
Invested in Capital Assets, Net of Related Debt	198,354	9,413	4,948	212,715	44,528
Restricted:					
Debt Service	23,411	3,225		26,636	
Unrestricted	7,678	1,085	(504)	8,259	(327)
Total Net Assets	\$ 229,443	\$ 13,723	\$ 4,444	\$ 247,610	\$ 44,201
Adjustment to reflect the consolidation of internal service fund activities related to enterprise funds.					(6,540)
Net assets of business-type activities					\$ 241,070

The accompanying notes are an integral part of these basic financial statements.

The accompanying notes are an integral part of these basic financial statements.

— CITY OF SAN ANTONIO, TEXAS —

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS

PROPRIETARY FUNDS

YEAR ENDED SEPTEMBER 30, 2005

(In Thousands)

	BUSINESS-TYPE ACTIVITIES ENTERPRISE FUNDS			NONMAJOR ENTERPRISE FUND-		TOTAL	INTERNAL SERVICE FUNDS
	AIRPORT SYSTEM	PARKING FACILITIES	ENVIRONMENTAL SERVICES				
Operating Revenues							
Charges for Services	\$ 45,791	\$ 10,325	\$ 51,753		\$ 107,869	\$ 183,422	
Total Operating Revenues	<u>45,791</u>	<u>10,325</u>	<u>51,753</u>		<u>107,869</u>	<u>183,422</u>	
Operating Expenses							
Personnel Services	17,421	3,885	22,508		43,814	32,364	
Contractual Services	2,881	686	19,558		23,125	12,073	
Commodities	745	148	1,878		2,771	4,227	
Materials						16,740	
Other	5,303	999	10,935		17,237	100,482	
Depreciation	8,874	780	369		10,023	12,351	
Total Operating Expenses	<u>35,224</u>	<u>6,498</u>	<u>55,248</u>		<u>96,970</u>	<u>178,737</u>	
Operating Income (Loss)	<u>10,567</u>	<u>3,827</u>	<u>(3,495)</u>		<u>10,899</u>	<u>4,685</u>	
Nonoperating Revenues (Expenses)							
Interest and Other	4,788	461	185		5,434	1,387	
Other Nonoperating Revenue	9,145	24	793		9,962	3,491	
Gain (Loss) on Sale of Capital Assets	10		86		96	1,507	
Interest and Debt Expense	(11,262)	(1,981)	(20)		(13,263)	(46)	
Other Nonoperating Expense	(549)				(549)		
Total Nonoperating Revenues (Expenses)	<u>2,132</u>	<u>(1,496)</u>	<u>1,044</u>		<u>1,680</u>	<u>6,339</u>	
Change in Net Assets Before Contributions and Transfers	<u>12,699</u>	<u>2,331</u>	<u>(2,451)</u>		<u>12,579</u>	<u>11,024</u>	
Capital Contributions	2,223				2,223		
Transfers In (Out)							
Transfers In		499	515		1,014	5,886	
Transfers Out	(615)	(1,027)	(1,522)		(3,164)	(2,946)	
Total Transfers	<u>(615)</u>	<u>(528)</u>	<u>(1,007)</u>		<u>(2,150)</u>	<u>2,940</u>	
Change in Net Assets	<u>14,307</u>	<u>1,803</u>	<u>(3,458)</u>		<u>12,652</u>	<u>13,964</u>	
Net Assets, Beginning	<u>215,136</u>	<u>11,920</u>	<u>7,902</u>			<u>30,237</u>	
Net Assets, Ending	<u>\$ 229,443</u>	<u>\$ 13,723</u>	<u>\$ 4,444</u>			<u>\$ 44,201</u>	
Adjustment to reflect the consolidation of internal service fund activities related to enterprise funds.							
Change in net assets of business-type activities.							

The accompanying notes are an integral part of these basic financial statements.

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STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
YEAR ENDED SEPTEMBER 30, 2005
(In Thousands)

	BUSINESS-TYPE ACTIVITIES ENTERPRISE FUNDS				GOVERNMENTAL ACTIVITIES	
	AIRPORT SYSTEM	PARKING FACILITIES	NONMAJOR ENTERPRISE FUND- ENVIRONMENTAL SERVICES	TOTALS	INTERNAL SERVICE FUNDS	
<u>Cash Flows from Operating Activities</u>						
Cash Received from Customers	\$ 45,114	\$ 10,213	\$ 51,672	\$ 106,999	\$	\$ 183,877
Cash Payments to Suppliers for Goods and Services	(6,470)	(1,748)	(31,827)	(40,045)		(131,953)
Cash Payments to Employees for Service	(17,359)	(3,865)	(22,364)	(43,588)		(32,100)
Net Cash Provided by (Used for) Operating Activities	21,285	4,600	(2,519)	23,366		19,824
<u>Cash Flows from Noncapital Financing Activities</u>						
Other Nonoperating Revenues	9,145	24	793	9,962		3,492
Transfers In from Other Funds		(1,027)	515	(512)		5,886
Transfers Out to Other Funds	(615)	499	(1,522)	(1,638)		(2,946)
Due to Other Funds	4,956	12,909	(419)	17,446		(9,058)
Due from Other Funds	(6,207)	(13,604)	409	(19,402)		10,218
Net Cash Provided by (Used for) Noncapital Financing Activities	7,279	(1,199)	(224)	5,856		7,592
<u>Cash Flows from Capital and Related Financing Activities</u>						
Acquisitions and Construction of Capital Assets	(18,615)	(1,259)	(481)	(20,355)		(19,244)
Proceeds from Issuance of Long-Term Debt	39,388	226		39,614		(91)
Principal Payments on Long-Term Debt	(8,390)	(1,580)	(143)	(10,113)		
Interest Paid on Long-Term Debt	(10,890)	(1,694)	(21)	(12,605)		
Debt Issuance Costs	(971)			(971)		662
Principal Payments on Notes						(46)
Interest Paid on Notes	10		109	119		2,971
Proceeds from Sale of Assets	532	(4,307)	(536)	(4,311)		(15,748)
Net Cash Provided by (Used for) Capital and Related Financing Activities						
<u>Cash Flows from Investing Activities</u>						
Purchases of Investment Securities	(394,347)	(24,765)	(2,218)	(421,330)		(82,820)
Maturity of Investment Securities	373,376	26,222	4,898	404,496		69,181
Investment Earnings	3,847	391	150	4,388		1,112
Net Cash Provided by (Used for) Investing Activities	(17,124)	1,848	2,830	(12,446)		(12,527)
Net Increase (Decrease) in Cash and Cash Equivalents	11,972	942	(449)	12,465		(859)
Cash and Cash Equivalents, October 1	8,397	2,469	741	11,607		5,566
Cash and Cash Equivalents, September 30	\$ 20,369	\$ 3,411	\$ 292	\$ 24,072	\$	\$ 4,707

The accompanying notes are an integral part of these basic financial statements.

— CITY OF SAN ANTONIO, TEXAS —

STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
YEAR ENDED SEPTEMBER 30, 2005
(In Thousands)

	BUSINESS-TYPE ACTIVITIES				GOVERNMENTAL	
	ENTERPRISE FUNDS				ACTIVITIES	
	AIRPORT SYSTEM	PARKING FACILITIES	ENVIRONMENTAL SERVICES	TOTALS	INTERNAL SERVICE FUNDS	
<u>Reconciliation of Operating Income to Net Cash</u> <u>Provided by (Used for) Operating Activities</u>						
Operating Income (Loss)	\$ 10,567	\$ 3,827	\$ (3,495)	\$ 10,899	\$	4,685
Adjustments to Reconcile Operating Income (Loss) to Net Cash Provided by (Used for) Operating Activities:						
Depreciation	8,874	780	370	10,024		12,351
Changes in Assets and Liabilities:						
(Increase) Decrease In Other Accounts Receivable	(376)	(55)	(15)	(446)		(53)
(Increase) Decrease In Allowance for Uncollectibles	3	(57)		(54)		9
(Increase) Decrease In Accrued Revenues	(32)		(66)	(98)		553
(Increase) In Due from Other Gov't. Agencies						(81)
(Increase) Decrease In Materials and Supplies	(165)	(10)	3	(172)		(434)
(Increase) Decrease In Prepaid Expenses	1			1		(726)
(Increase) In Deposits						(124)
Decrease In Vouchers Payable	397	59	1,169	1,625		3,966
Increase (Decrease) In Other Payables	2,226	36	(629)	1,633		(586)
Increase In Accrued Payroll	66	29	104	199		223
Increase (Decrease) In Accrued Leave Payable	(4)	(9)	40	27		41
(Decrease) In Unearned Revenue	(272)			(272)		
<u>Net Cash Provided by (Used for) Operating Activities</u>	<u>\$ 21,285</u>	<u>\$ 4,600</u>	<u>\$ (2,519)</u>	<u>\$ 23,366</u>	<u>\$</u>	<u>19,824</u>
<u>Noncash Investing, Capital and Financing Activities:</u> <u>Acquisitions and Construction of Capital Assets</u> <u>from Capital Contributions</u>	\$ 2,223	\$	\$	\$ 2,223	\$	

The accompanying notes are an integral part of these basic financial statements.

— CITY OF SAN ANTONIO, TEXAS —

STATEMENT OF FIDUCIARY NET ASSETS/BALANCE SHEET

FIDUCIARY FUNDS

AS OF SEPTEMBER 30, 2005

(In Thousands)

ASSETS	FIRE AND POLICE PENSION AND HEALTHCARE FUNDS	PRIVATE PURPOSE TRUST FUNDS	AGENCY FUNDS
Current Assets			
Cash and Cash Equivalents	\$ 110,707	\$ 2	\$ 7,186
Security Lending Collateral	177,712		
Investments, at Fair Value:		29	947
U.S. Government and Agency Issues	205,413		
Corporate Bonds	85,628		
Preferred Common Stock	68,448		
Other	1,381,748		
Total Investments, at Fair Value	1,741,237	29	947
Receivables:			
Other Accounts	4,571		384
Accrued Interest	4,785		7
Accrued Revenue	1,441		
Prepayments	13		
Total Current Assets	2,040,466	31	8,524
Capital Assets			
Computer Equipment	76		
Buildings	590		
Total Capital Assets	666		
Less: Accumulated Depreciation	344		
Net Capital Assets	322		
Total Assets	2,040,788	31	8,524
LIABILITIES			
Vouchers Payable	4,724		1
Accounts Payable- Other	4,296		7,823
Accrued Payroll	76		
Due to Other Funds			700
Unearned Revenue	355		
Securities Lending	177,712		
Total Liabilities	187,163		8,524
NET ASSETS			
Held in Trust for Pension Benefits and Other Purposes	\$ 1,853,625	\$ 31	

The accompanying notes are an integral part of these basic financial statements.

— CITY OF SAN ANTONIO, TEXAS —

STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS

FIDUCIARY FUNDS

YEAR ENDED SEPTEMBER 30, 2005

(In Thousands)

	FIRE AND POLICE PENSION AND HEALTHCARE FUNDS	PRIVATE PURPOSE TRUST FUNDS
ADDITIONS:		
Contributions:		
Employer	\$ 69,602	\$ -
Employee	25,422	
Other Contributions		3
Total Contributions	95,024	3
Investment Earnings:		
Net Increase in Fair Value of Investments	189,534	
Real Estate Income, Net	2,160	
Interest and Dividends	39,256	1
Securities Lending	4,606	
Other Income	795	
Total Investment Earnings	236,351	1
Less Investment Expenses:		
Investment Management Fees and Custodian Fees	(8,852)	
Securities Lending Expenses:		
Borrower Rebates	(4,052)	
Lending Fees	(194)	
Net Investment Income	223,253	1
Total Additions	318,277	4
DEDUCTIONS:		
Benefits	82,800	
Refunds of Contributions	510	
Administrative Expense	1,690	5
Salaries, Wage, and Employee Benefits	555	
Total Deductions	85,535	5
Change in Net Assets	232,742	(1)
Net Assets, Beginning	1,620,883	32
Net Assets, End	\$ 1,853,625	\$ 31

The accompanying notes are an integral part of these basic financial statements.

STATEMENT OF NET ASSETS
COMPONENT UNITS
AS OF SEPTEMBER 30, 2005
(In Thousands)

ASSETS	SAN ANTONIO			CITY		NONMAJOR		TOTAL
	WATER	PUBLIC	SYSTEM	SERVICE	UNITS	COMPONENT	UNITS	
Current Assets:								
Cash and Cash Equivalents	\$	\$	\$	\$	\$	\$	\$	\$
Investments	43,542	50,920		258,406	16,238	8,596		67,138
Receivables, net:								310,854
Notes								12,200
Other Accounts	32,037	161,419			3,947			197,403
Accrued Interest	1,211	2,629			57			3,897
Materials and Supplies, at Cost	4,538	115,272			49			119,859
Due from Other Governmental Agencies					3,530			3,530
Prepaid Expenses	3,035	30,951			515			34,501
Total Current Assets	84,363	619,597			43,442			749,402
Noncurrent Assets:								
Restricted Assets:								
Debt Service Accounts:								
Cash and Cash Equivalents	73	738						811
Investments	18,785							18,785
Construction Accounts:								
Cash and Cash Equivalents								108,993
Investments	15,738	93,255						250,012
Repair and Replacement Account:								
Investments	205,161	44,851						572,057
Receivables-Accrued Interest								4,948
Conservation Accounts:								
Investments	2,503							2,503
Other Restricted Accounts:								
Cash and Cash Equivalents		26,300			5,510			31,810
Investments	21,966	378,924						400,890
Receivables-Accrued Interest		2,643						2,643
Total Restricted Assets	264,226	1,123,716			5,510			1,393,452
Capital Assets:								
Land	82,339	56,482						151,355
Infrastructure					12,524			42,580
Buildings					167,449			9,298,902
Utility Plant in Service	2,293,502	7,005,400			2,247			105,299
Machinery and Equipment	103,052	180,594			14,755			704,711
Construction in Progress	509,362	319,186						18,785
Utility Property Leased								319,186
Nuclear Fuel - Net		12,599						12,599
Non-utility Property - Land		7,593,046			239,565			10,820,866
Total Capital Assets	2,988,255	15,002,926			39,589			3,785,098
Less: Accumulated Depreciation	798,457	2,947,052			199,976			7,035,768
Net Capital Assets	2,189,798	4,645,994						
Assets Held for Resale								
Prepaid Rent Long Term-Leaseback	8,210	516,182						8,210
Unamortized Debt Expense	10,660	27,001						516,182
Total Noncurrent Assets	2,472,894	6,312,893			205,486			37,661
Total Assets	2,557,257	6,932,490			250,928			8,991,273
	\$	\$	\$	\$	\$	\$	\$	\$

The accompanying notes are an integral part of these basic financial statements.

STATEMENT OF NET ASSETS
COMPONENT UNITS
AS OF SEPTEMBER 30, 2005
(In Thousands)

LIABILITIES	SAN ANTONIO			CITY		NONMAJOR		TOTAL
	WATER	PUBLIC	SYSTEM	SERVICE	UNITS	COMPONENT	UNITS	
Current Liabilities:								
Accounts Payable and Other Current Liabilities	\$	\$	\$	\$	\$	\$	\$	\$
Sewer Collections Payable	256				12,380			225,202
Unearned Revenues								1,897
Notes Payable	627				1,897			2,954
Due to Other Governmental Agencies					1,108			1,108
Total Current Liabilities (Payable from Current Assets)	29,267	184,238			17,912			231,417
Current Liabilities (Payable from Restricted Assets):								
Accrued Bond and Certificate Interest	7,151							7,151
Current Portion of Bonds and Certificates	16,505	127,255						143,760
Other Payables	16,949				2,345			19,294
Total Current Liabilities (Payable from Restricted Assets)	40,605	127,255			2,345			170,205
Total Current Liabilities	69,872	311,493			20,257			401,622
Noncurrent Liabilities:								
Revenue Bonds (Net of Current Portion)	1,145,905	2,533,970						3,679,875
Commercial Paper	238,400	350,000						588,400
Unamortized Premium on New Series Bonds	9,078	89,149						98,227
Plus: Unamortized Discount on New Series Bonds	(14,382)	(14,382)						(14,382)
Deferred Amount on Refunding	(22,727)	(134,227)						(156,954)
Long-Term Lease/Notes Payable	1,388	588,455			87,268			677,111
Other Payables	1,879	308,049			1,095			311,023
Total Noncurrent Liabilities	1,359,541	3,733,396			88,363			5,183,300
Total Liabilities	1,429,413	4,046,889			108,620			5,584,922
NET ASSETS								
Invested in Capital Assets,								
Net of Related Debt	1,041,888	1,821,531			112,756			2,976,175
Restricted for Renewal and Replacement		577,005			2,400			579,405
Restricted for Debt Service	11,706	738			4,810			17,254
Restricted for Conservation	2,504	172,752			140			175,396
Temporarily Restricted					141			141
Unrestricted	71,746	313,575			22,061			407,382
Total Net Assets	1,127,844	2,885,601			142,308			4,155,753
	\$	\$	\$	\$	\$	\$	\$	\$

The accompanying notes are an integral part of these basic financial statements.

STATEMENT OF ACTIVITIES
COMPONENT UNITS
YEAR ENDED SEPTEMBER 30, 2005
(In Thousands)

	Program Revenues			Net (Expense) Revenue and Changes In Net Assets		
	EXPENSES	CHARGES FOR SERVICES	CAPITAL GRANTS AND CONTRIBUTIONS	SAN ANTONIO WATER SYSTEM	CITY PUBLIC SERVICE	NONMAJOR COMPONENT UNITS
San Antonio Water System	\$ 265,029	\$ 262,687	\$ 59,742	\$ 57,400	\$	\$ 57,400
City Public Service	1,465,600	1,422,405	47,666		4,471	4,471
Nonmajor Component Units	53,747	14,039	38,409		(1,299)	(1,299)
Total	\$ 1,784,376	\$ 1,699,131	\$ 145,817	\$ 57,400	4,471	60,572
General Revenues:						
Investment Earnings				7,060	49,327	57,352
Miscellaneous					2,427	13,345
Gain on Disposal of Capital Assets				131		5,262
Total General Revenues				7,191	51,754	75,959
Change in Net Assets				64,591	56,225	136,531
Net Assets, Beginning				1,058,186	2,829,376	4,014,155
Prior Period Adjustment				5,067		5,067
Net Assets, Ending				\$ 1,127,844	\$ 2,885,601	\$ 4,155,753

The accompanying notes are an integral part of these basic financial statements.

**TABLE OF NOTES TO FINANCIAL STATEMENTS
YEAR ENDED SEPTEMBER 30, 2005**

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1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the City of San Antonio (City) have been prepared in conformance with U.S. generally accepted accounting principles (GAAP) for local governmental units. The Governmental Accounting Standards Board (GASB) is the accepted body for establishing governmental accounting and financial reporting standards. The following is a summary of significant accounting policies of the City.

A. Reporting Entity

In the evaluation of how to define the City for financial reporting purposes, management considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the criteria set forth in GASB Statement No. 14, *The Financial Reporting Entity*, as amended by GASB Statement No. 39, *Determining Whether Certain Organizations Are Component Units—an amendment of GASB Statement No. 14*. The underlying concept of the financial reporting entity is that elected officials are "accountable" to their constituents for their actions. One of the objectives of this concept is to provide users of governmental financial statements with a basis for assessing the accountability of those elected officials, and accordingly, the definition of the financial reporting entity is based on accountability.

The financial reporting entity consists of: (a) the primary government (in these financial statements the primary government is the City), (b) component units, which are legally separate organizations for which the City is financially accountable (blended), and (c) component units, which the nature and significance of their relationship with the City is such that exclusion from the reporting entity's financial statements would be misleading or incomplete (discretely presented).

Using the criteria of GASB Statement No. 39 and Statement No. 14 outlined below, potential component units were evaluated for inclusion in or exclusion from the reporting entity, whether the organizations were financially accountable or not, and were further evaluated for financial statement presentation. Based on their individual relationships with the City, some component unit financial statements were blended as though they are part of the City and others only discretely presented.

The following criteria (as set forth in GASB Statement No. 14 and Statement No. 39) were used in the evaluation of potential component units of the City:

- 1) Legally separate
- 2) Financial accountability
 - a) Appointment of a voting majority
 - b) Imposition of will
 - c) Financial benefit to or burden on the City
 - d) Fiscal dependency
- 3) The relationship with the City is such that exclusion would cause these financial statements to be misleading or incomplete.
- 4) Service rendered by the potential component unit is provided entirely or almost entirely to the City.
- 5) The City, or its component units, are entitled to, or have the ability to access, the majority of the resources received or held by the separate organization.

(amounts are expressed in thousands)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

A. Reporting Entity (Continued)

The criteria outlined above were excerpted from GASB Statement No. 14 and Statement No. 39. For a more detailed explanation of the criteria established by the statements, the reader is referred to the Codification of Governmental Accounting and Financial Reporting Standards, as of June 30, 2004, published by GASB, Section 2600. GASB Statement No. 39 further clarifies that a not-for-profit may not be financially accountable to the City, but may be considered a component unit based on the nature and significance of their relationship with the City. Predicated upon the application of the criteria outlined above, the following is a brief overview of component units included in the reporting entity:

Blended with the Primary Government (the relationship among the following component units and the City meet the criteria, as set forth in GASB Statement No. 14 and Statement No. 39, for inclusion in the Reporting Entity and is such that the financial statements are blended in with those of the City):

As set forth in GASB Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, the City excludes fiduciary funds and component units that are fiduciary in nature from the government-wide financial statements. The City's component units that are fiduciary in nature are the San Antonio Fire and Police Pension Fund and the San Antonio Fire and Police Retiree Health Care Fund. These component units are presented in the Statements of Fiduciary Net Assets and Changes in Fiduciary Net Assets.

City of San Antonio Health Facilities Development Corporation

The City of San Antonio Health Facilities Development Corporation (HFDC) was established by Ordinance No. 55400, dated June 3, 1982, in accordance with state laws for the purposes of, and to act on behalf of the City as a health facilities development corporation under the Texas Health Facilities Development Act of 1981. The HFDC is authorized to issue tax-exempt health facility revenue bonds, for which the City is not obligated in any manner to finance health related projects in support of the promotion, expansion, and improvement of health facilities. The HFDC is governed by a Board of Directors, which is comprised of the City Council of the City of San Antonio.

City of San Antonio Industrial Development Authority

The City of San Antonio Industrial Development Authority (IDA) was established by Resolution No. 79-48-100 dated October 11, 1979, in accordance with state laws for the purposes of benefiting and accomplishing public purposes of, and to act on behalf of the City as an industrial development corporation under the Development Corporation Act of 1979. The IDA is authorized to issue tax-exempt industrial revenue bonds, for which the City is not obligated in any manner, to finance qualified projects that may further the promotion and development of commercial, industrial, and manufacturing enterprises to advance and encourage employment and the public welfare. The IDA is governed by a Board of Directors, which is comprised of the City Council of the City of San Antonio.

San Antonio Fire and Police Pension Fund

The San Antonio Fire and Police Pension Fund (Pension Fund) is a Single Employer Defined Benefit Plan established in accordance with state law. The Pension Fund is administered by a nine-member Board of Trustees, including three City Council members. The City and Pension Fund participants are obligated to make all contributions to the Pension Fund in accordance with rates established by state law. Benefit levels are also set by state law. Services rendered by the Pension Fund are exclusively for the benefit of eligible firefighters and police officers upon retirement.

(amounts are expressed in thousands)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

A. Reporting Entity (Continued)

San Antonio Fire and Police Retiree Health Care Fund

The City of San Antonio Firefighters' and Police Officers' Retiree Prefunded Group Health Plan was created in October 1989, in accordance with the provisions of the City's contracts with the local fire and police unions, respectively, to provide postemployment healthcare benefits to uniformed employees who retired on or after October 1, 1989. Pursuant to the passage of Senate Bill 1568 in 1997, a separate and distinct statutory trust, the Fire and Police Retiree Health Care Fund (Health Fund), was created to provide these postemployment healthcare benefits for eligible uniformed employees of the City. The Health Fund is administered by a nine-member board of trustees, including three City Council Members, and is funded primarily by contributions from the City and contributions made by active employees and retirees on behalf of their dependents. The City and active employee and retiree contribution rates are established pursuant to the Fire and Police collective bargaining agreements.

City of San Antonio Texas Municipal Facilities Corporation

The City of San Antonio Texas Municipal Facilities Corporation (TMFC) was established in fiscal year 2001 in accordance with state law for the purposes of, and to act on behalf of the City in acquiring, constructing, equipping, financing, operating, and maintaining land and other municipal facilities for the City. The TMFC is governed by a Board of Directors, which is comprised of the City Council of the City of San Antonio.

City of San Antonio Texas Starbright Industrial Development Corporation

The City of San Antonio Texas Starbright Industrial Development Corporation (TSIDC) was established in fiscal year 2003 in accordance with state law for the purposes of, and to act on behalf of the City in the promotion and development of commercial, industrial, and manufacturing enterprises, to advance and encourage employment and the public welfare, including but not limited to the acquisition of land. The TSIDC is governed by a Board of Directors, which is comprised of the City Council of the City of San Antonio.

City of San Antonio Texas Convention Center Hotel Finance Corporation

The City of San Antonio, Texas Convention Center Hotel Finance Corporation (TCHFC) was established in fiscal year 2005 in accordance with the state law for the purposes of, and to act on behalf of City local economic development and stimulate business and commercial activity in the City. The TCHFC is governed by a Board of Directors, which is comprised of the City Council of the City of San Antonio.

Discretely Presented With the Primary Government (the relationship among the following component units and the City is such that they meet the criteria, as set forth in GASB Statement No. 14 and Statement No. 39, for inclusion in the reporting entity, and accordingly are included; however, are such that the financial statements are discretely presented alongside, but not blended with those of the City):

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(amounts are expressed in thousands)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

A. Reporting Entity (Continued)

San Antonio Water System

On February 13, 1992, the City Council determined it was in the best interest of the citizens of San Antonio and the customers served by the water and wastewater utilities to consolidate all water utilities, agencies, and activities into one institution. It was determined that the best mechanism for effecting the consolidation of all water systems, agencies, and activities into a single institution was through a refunding of all the then outstanding water and sewer bonds. The consolidation was consummated on May 19, 1992, with the creation of the San Antonio Water System (SAWS) that included the former City Water Board, Alamo Water Conservation and Re-use District, and the City's Sewer and Stormwater system.

It was further determined by the City Council that the interests of the citizens and customers would best be served by placing authority for management and control of SAWS, as consolidated, in a Board of Trustees. This Board of Trustees includes the City's Mayor as an ex-officio member, along with six members appointed by the City Council for four-year staggered terms. The user rates for user charges and bond issuance authorizations are approved by the City Council.

City Public Service

City Public Service (CPS), a municipally owned utility, provides electricity and natural gas to San Antonio and the surrounding areas. CPS is governed by a Board of Trustees, which is comprised of four members appointed by City Council and the Mayor of the City as an ex-officio member. The user rates for user charges and bond issuance authorizations are approved by the City Council.

San Antonio Development Agency

The San Antonio Development Agency (SADA) was created under the provisions of the Urban Renewal Law of the State of Texas. SADA is responsible for implementing the City's Urban Renewal Program and may designate for urban renewal such areas as it deems advisable, subject to approval by the City Council and the Federal Agency, which administers the overall program. SADA receives a majority of its operating funds from the City as pass-through grant funds and is governed by a seven-member Board of Commissioners appointed by the City Council.

San Antonio Education Facilities Corporation

The City of San Antonio Higher Education Authority (SAHEA) was established in 1984, in accordance with state laws for the purpose of aiding non-profit institutions of higher education in providing educational, housing, and other related facilities in accordance with and subject to the provisions of Section 53.35 (b) Texas Education Code, all to be done on behalf of the City and as its duly constituted authority and instrumentality. In 2001, the SAHEA changed its name to the San Antonio Education Facilities Corporation (SAEFC). The Act authorizes the SAEFC to issue revenue bonds for these purposes on behalf of the City, but the bonds are not obligations of the City. SAEFC is governed by an eleven-member Board of Directors appointed by the City Council for two-year terms. Board members are subject to removal by the City Council for cause or at will, and the City reserves the right to terminate and dissolve the SAEFC at any time.

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(amounts are expressed in thousands)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

A. Reporting Entity (Continued)

Greater Kelly Development Authority

The Greater Kelly Development Corporation (GKDC) was established in 1996 as the local development authority on an interim basis under the Development Corporation Act of 1979 for the development and redevelopment of Kelly Air Force Base (Kelly). In November 1999, the City established the Greater Kelly Development Authority (GKDA) as the successor-in-interest to the GKDC pursuant to the newly enacted Senate Bill 655. In accordance with the Act, the GKDA has the powers previously enjoyed by the GKDC while at the same time clarifying such powers and preserving the property tax-exempt status of prior commercial tenants at Kelly. The GKDA is a special district and political subdivision of the State of Texas and was established for the purpose of monitoring the proposed closing of Kelly; conducting comprehensive studies of all issues related to the closure, conversion, redevelopment, and future use of Kelly; reviewing all options relative to the most appropriate uses of Kelly and the surrounding area; formulating and adopting a comprehensive plan for the conversion and redevelopment of Kelly and submitting such plan to the appropriate agency or agencies of the federal government; and implementing such plan as it relates to Kelly and the surrounding area. The GKDA is governed by an eleven-member Board of Directors, appointed by the City Council. The City Council also has the ability to remove appointed members of the organization's governing board at will. The GKDA is authorized to issue bonds to finance any project as permitted by Texas Law, but said bonds are not obligations of the City.

San Antonio Housing Trust Foundation, Inc.

The San Antonio Housing Trust Foundation, Inc. (SAHTF) is a non-profit corporation incorporated in 1990 under the laws of the State of Texas. SAHTF was organized for the purposes of supporting charitable, educational, and scientific undertakings, and specifically for providing housing for low and middle-income families, and to provide administrative and other support for the operations of the City of San Antonio Housing Trust Fund, a Permanent Fund of the City. The Housing Trust Fund was established by the City for the purposes of providing additional and continuing housing opportunities for low and moderate-income families; promoting public health, safety, convenience, and welfare; and revitalizing neighborhoods and the downtown area through appropriate housing activities. SAHTF is governed by an eleven-member Board of Directors appointed by the City Council. SAHTF administers The San Antonio Housing Trust Finance Corporation. The City has the ability to appoint, hire, reassign, or dismiss those persons responsible for the day-to-day operations of the SAHTF as it authorizes a contract for the administration and management of the operations on an annual basis.

San Antonio Local Development Company, Inc. dba South Texas Business Fund (STBF)

The San Antonio Local Development Company Inc. (SALDC) is a non-profit corporation organized in 1978 under the laws of the State of Texas and the auspices of the City. In 2004, SALDC changed its name to the San Antonio Local Development Company dba South Texas Business Fund (STBF). The STBF also expanded the area served from twelve counties to all of the counties in the State of Texas. STBF was formed to participate in the Neighborhood Business Revitalization Program (NBRP), which is co-sponsored by the Small Business Administration (SBA), the Economic Development Administration, and the U.S. Department of Housing and Urban Development (HUD). STBF is governed by a thirty-three member Board of Trustees, appointed by the City Council, and an eleven-member Board of Directors appointed from the Board of Trustees. STBF, under agreement with the City, administers and operates a revolving loan fund, NBRP, that provides qualifying local businesses with loans under economic development programs administered by the SBA. STBF also administers, by agreement with the City, a U.S. Department of Commerce Title IX Revolving Loan Fund, SBA MicroLoan Program, and a HUD 108 Fund. Currently, STBF has an outstanding note payable to HUD, which is guaranteed by the City.

(amounts are expressed in thousands)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

A. Reporting Entity (Continued)

Brooks Development Authority

The Brooks Development Authority (BDA) is a special district and political subdivision of the State of Texas. It was established on September 27, 2001, as a defense base development authority in accordance with state law for the purposes of, and to act on behalf of the City in improving mission effectiveness, reducing the cost of providing quality installation support through improved capital asset management, and promoting economic development on Brooks Air Force Base and in the surrounding community. An eleven-member Board of Directors appointed by the City Council, governs the BDA for two-year terms and will oversee the Brooks Technology and Business Park in support of the Brooks City-Base Project. The City has the ability to impose its will on this organization as the City Council has the power to remove board members by adopting a resolution.

Essential disclosures related to the above mentioned discretely presented and blended component units are included in the complete financial statements of each of the individual component units. These statements may be obtained at the respective entity's administrative office. The addresses are as follows:

Discretely Presented Component Units

San Antonio Water System P.O. Box 2449 San Antonio, Texas 78298-2449 Contact Person: Doug Evanson Telephone No. (210) 233-3803	City Public Service P.O. Box 1771 San Antonio, Texas 78296-1771 Contact Person: Richard E. Williamson Telephone No. (210) 353-2397
San Antonio Development Agency P.O. Box 831386 San Antonio, Texas 78283-1386 Contact Person: Felix Lopez Telephone No. (210) 207-5444	San Antonio Education Facilities Corporation P.O. Box 830504 San Antonio, Texas 78283-0504 Contact Person: Ramiro Cavazos Telephone No. (210) 207-8040
Greater Kelly Development Authority 143 Billy Mitchell Blvd., Ste 6 San Antonio, Texas 78226-1816 Contact Person: Bruce Miller Telephone No. (210) 362-7800	San Antonio Housing Trust Foundation, Inc. 2515 Blanco Rd. San Antonio, Texas 78212-2796 Contact Person: John Kenny Telephone No. (210) 735-2772
San Antonio Local Development Company Inc. dba South Texas Business Fund P.O. Box 830505 San Antonio, Texas 78283-0505 Contact Person: Ramiro Cavazos Telephone No. (210) 207-8040	Brooks Development Authority 8030 Challenger Drive Brooks City-Base, Texas 78235-5355 Contact Person: Bart Sanchez Telephone No. (210) 536-6710

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(amounts are expressed in thousands)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

A. Reporting Entity (Continued)

Blended Component Units

San Antonio Health Facilities Development Corporation P.O. Box 830504 San Antonio, Texas 78283-0504 Contact Person: Ramiro Cavazos Telephone No. (210) 207-8040	San Antonio Industrial Development Authority P.O. Box 830504 San Antonio, Texas 78283-0504 Contact Person: Ramiro Cavazos Telephone No. (210) 207-8040
San Antonio Fire and Police Retiree Health Care Fund 300 Convent Street, Suite 2500 San Antonio, Texas 78205-3716 Contact Person: James Bounds Telephone No. (210) 220-1385	San Antonio Fire and Police Pension Fund 311 Roosevelt San Antonio, Texas 78210-2700 Contact Person: Warren Schott Telephone No. (210) 534-3262
San Antonio Texas Convention Center Hotel Finance Corporation 100 Military Plaza 4 th Floor, City Hall San Antonio, Texas 78205-2425 Contact Person: Ramiro Cavazos Telephone No. (210) 207-8040	San Antonio Texas Municipal Facilities Corporation P.O. Box 839966 San Antonio, Texas 78283-3966 Contact Person: Ben Gorzell Jr. Telephone No. (210) 207-8620

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(amounts are expressed in thousands)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

A. Reporting Entity (Continued)

It is management's belief that to exclude essential disclosures from the City's financial statements as they pertain to CPS and SAWS would be misleading. CPS and SAWS have been identified as major discretely presented component units both as they relate to total component units and to the primary government. Therefore, relevant disclosures have been included in the City's financial statements. Discretely presented component units with different fiscal year ends from the City are the San Antonio Water System with a fiscal year-end of December 31, and City Public Service with a fiscal year-end of January 31.

Related Organizations

The City Council appoints the members to the Board of Directors for the San Antonio Housing Authority; however, the City's accountability for this entity does not extend beyond making appointments to the Board of Directors and the coordination and approval of strategic plans.

B. Basic Financial Statements – GASB Statement No. 34

Effective October 1, 2001, the City implemented the provisions of GASB Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*. In fiscal year 2003, the City implemented the portion of GASB Statement No. 38, *Certain Financial Statement Note Disclosures*, relating to the disaggregation of receivable and payable balances. These statements comply with the requirements of the new reporting model.

Government-wide and Fund Financial Statements

The basic financial statements include three components: (1) government-wide financial statements, (2) fund financial statements, and (3) notes to the financial statements. The government-wide financial statements report information on all non-fiduciary activities of the primary government and its component units. Management's Discussion and Analysis introduces the basic financial statements and provides an analytical overview of the City's financial activities. As part of the implementation of GASB Statement No. 34, the City has early implemented requirements for infrastructure reporting. GASB Statement No. 34 requires the historical cost of infrastructure assets, retroactive to 1980, to be included as part of the capital assets, as well as the related depreciation, to be reported in the government-wide financial statements. In addition, for the most part, the effect of interfund activity has been removed from the statements.

The Statement of Net Assets reflects both short-term and long-term assets and liabilities. In the Government-wide Statement of Net Assets governmental activities are reported separately from business-type activities. Governmental activities are supported by taxes and intergovernmental revenues, whereas business-type activities are normally supported by fees and charges for services. Long-term assets, such as capital assets, infrastructure assets, and long-term obligations are now reported with the assets of governmental activity. The components of net assets, previously shown as fund balances, are presented in three separate components; 1) Invested in Capital Assets, net of related debt, 2) Restricted, and 3) Unrestricted. Interfund receivables and payables between governmental and business-type activities have been eliminated in the government-wide Statement of Net Assets, which minimizes the duplication of assets and liabilities within the governmental and business-type activities. Component units are also reported in the Statement of Net Assets.

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(amounts are expressed in thousands)

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Basic Financial Statements – GASB Statement No. 34 (Continued)

Government-wide and Fund Financial Statements (Continued)

The Statement of Activities reflects both the gross and net cost format. The net cost (by function or business-type activity) is usually covered by general revenues (property tax, sales tax, intergovernmental revenues, etc.). Direct (gross) expenses of a given function or segment are offset by program revenue, and operating and capital grants. Program revenues must be directly associated with the function of business-type activity. The presentation allows users to determine which functions are self-supporting, and which rely on the tax base in order to complete their mission. Internal service fund balances, whether positive or negative, have been eliminated against the expenses and program revenues shown in the governmental and business-type activities of the Statement of Activities.

A reconciliation, detailing the change in net assets between the government-wide financial statements and the fund financial statements, is presented separately for governmental funds. In order to achieve a break-even result in the internal service fund activity, differences in the basis of accounting and reclassifications are allocated back to user departments. These allocations are reflected in the government-wide statements. Any residual amounts of the internal service funds are reported in the governmental activity column.

The proprietary funds have a reconciliation presented in the proprietary funds' Statement of Net Assets and Statement of Revenues, Expenses, and Changes in Fund Net Assets. The only reconciling item is the internal service fund allocation.

C. Fund Accounting

The accounts of the City are organized on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets and other debits, liabilities, fund equity and other credits, revenues and expenditures, or expenses, as appropriate. Government resources are allocated to and accounted for in individual funds based upon the purposes for which they are to be spent and the means by which spending activities are controlled. The City has three types of Funds: Governmental Funds, Proprietary Funds, and Fiduciary Funds. The Fund Financial Statements provide more detailed information about the City's most significant funds, but not on the City as a whole. Major individual governmental funds and major enterprise funds are reported separately in the Fund Financial Statements. Nonmajor funds are independently presented in the combining statements.

The criteria used to determine if a governmental or enterprise fund should be reported as a major fund is as follows: The total assets, liabilities, revenues, or expenditure/expenses of that individual governmental or enterprise fund are at least 10.0% of the corresponding element total for all funds of that category or type (that is, total governmental or total enterprise funds), and the same element that met the 10.0% criterion above in the individual governmental or enterprise fund is at least 5.0% of the corresponding element total for all governmental and enterprise funds combined.

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(amounts are expressed in thousands)

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

C. Fund Accounting (Continued)

The following is a brief description of the major governmental funds that are each presented in a separate column in the fund financial statements:

The General Fund is always presented as a major fund.

The Debt Service Fund accounts for the accumulation of resources for, and the payment of general long-term debt principal, interest, and related costs except that which is accounted for in proprietary-type funds.

The City of San Antonio Texas Convention Center Hotel Fund accounts for the selling of debt to finance the Convention Center Hotel building project.

The following is a brief description of the major enterprise funds that are each presented in a separate column in the fund financial statements:

The Airport System accounts for the operation of the San Antonio International Airport and Stinson Municipal Airport. Financing for the Airport System operations is provided by user fees.

The Parking System accounts for the operations of the City's parking facilities. Financing for the Parking Facilities operations is provided by user fees.

Governmental Funds

General Fund - The General Fund of the City is the primary operating fund, which accounts for all financial resources of the general government except those required to be accounted for in another fund.

Special Revenue Funds - Special Revenue Funds are used to account for the proceeds of specific revenue sources (other than private-purpose trusts and major capital projects) that are legally restricted to expenditures for specified purposes.

Debt Service Funds - Debt Service Funds are used to account for the accumulation of resources for, and the payment of, general long-term debt principal, interest and related costs.

Capital Projects Funds - Capital Projects Funds are used to account for the financial resources to be used for the acquisition or construction of major capital facilities (other than those financed by Proprietary Funds and Trust Funds).

Permanent Funds - Permanent Funds are used to report resources that are legally restricted to the extent that only earnings, and not principal, may be used for purposes that support the reporting government's programs - that is, for the benefit of the government or its citizenry.

The governmental funds, which have legally adopted budgets are the General Fund, Special Revenue Funds (excluding Project Management Office, HOME Program, Categorical Grant-In Aid, HUD 108 Loan Program, Community Development Program, Community Services, Advanced Transportation District, and Capital Project Funds), Official City Store Fund, San Jose Burial Fund, and the Debt Service Funds.

Proprietary Funds

Enterprise Funds - Enterprise Funds are used to account for operations that are financed and operated in a manner similar to private business enterprises where the intent of the governing body is that the cost (expenses, including depreciation) of providing goods or services to the general public on a continuing basis should be financed or recovered primarily through user charges.

(amounts are expressed in thousands)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

C. Fund Accounting (Continued)

Proprietary Funds (Continued)

Internal Service Funds - Internal Service Funds are used to account for the financing of goods or services provided by one department or agency to other departments or agencies of the City, or to other governmental units, on a cost-reimbursement basis. The City's self-insurance programs, data processing programs, and other internal service programs are accounted for in these funds.

Fiduciary Funds

Trust and Agency Funds - Trust and Agency Funds are used to account for assets held by the City in a trustee capacity or as an agent for individuals, private organizations, other governmental units, or other funds. These include Pension Trust, Retiree Health Care Trust, Private Purpose Trust Funds, and Agency Funds. Pension Trust, Retiree Health Care Trust, and Private Purpose Trust Funds are accounted for in essentially the same manner as proprietary funds since capital maintenance is critical. Agency Funds are custodial in nature (assets equal liabilities) and do not involve measurement of results of operations.

D. Measurement Focus and Basis of Accounting

The government-wide financial statements present information about the City as a whole. Government-wide financial statements exclude both fiduciary funds and fiduciary component units. The Statement of Net Assets and the Statement of Activities are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. The City recognizes revenue from property taxes in the period for which they were levied. Property taxes receivable includes taxes due and amounts expected to be collected within 60 days after the period end, along with related interest and penalties. For additional disclosure related to property taxes, see Note 2. Other taxes and fees are recognized as revenue in the year they are earned. Revenues from grants and similar items are recognized in the fiscal year the qualifying expenditures are made and all other eligibility requirements have been satisfied.

Program Revenues are presented in the Government-wide Statement of Activities. The City reports program revenues into three categories: 1) Charges for services, 2) Operating grants and contributions, and 3) Capital grants and contributions. Further descriptions of these three categories follow. They are presented separately as a reduction of the total expense to arrive at the net expense of each functional activity. Program revenues are revenues generated by transactions with outside parties who purchase, use, or directly benefit from a program. They also include amounts such as grants and contributions received from outside parties that restrict the use of those funds to specific programs. Investment earnings that are legally restricted to specific programs are also reported as program revenues.

1) Charges for services are revenues that are generated by those who purchase goods or services from the City. Examples of charges for services include airport landing fees, solid waste collection and disposal fees, vacant lot clean up, golf course fees, and food establishment licenses. Fines and forfeitures are also reported under charges for services.

2) Operating grants and contributions are those revenues that are restricted in the way they may be spent - either for operations of a particular program or to purchase a capital asset for a particular program.

3) Capital grants and contributions are also restricted revenues; the funds may only be spent to purchase capital assets for specified programs.

(amounts are expressed in thousands)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

D. Measurement Focus and Basis of Accounting (Continued)

All governmental funds are accounted for using the current financial resources measurement focus and the modified accrual basis of accounting. This means that only current assets and current liabilities are generally included on their balance sheets. Revenues are recognized in the accounting period in which they become available and measurable. For this purpose, the City considers revenues, other than grants, to be available if the revenues are collected within sixty days after year-end. Grant revenues are recognized when reimbursable expenditures are made and all other eligibility requirements imposed by the provider are met. Grant funds received in advance and delinquent property taxes are recorded as unearned revenue until earned and available. Gross receipts and sales taxes are considered available when in the hands of intermediary collecting governments, and are recognized at that time. Anticipated refunds of such taxes are recorded as liabilities and reductions of revenue when they are measurable and their validity seems certain. Expenditures are recognized in the accounting period in which the fund liability is incurred; however, compensated absences, debt service expenditures, claims and judgments, and arbitrage rebates are recorded only when the liability is matured.

The reported fund balance (net current assets) for each fund is considered a measure of "current financial resources." Governmental fund operating statements present increases (revenues and other financing sources) and decreases (expenditures and other financing uses) in net current assets. Accordingly, they are said to present a summary of sources and uses of "current financial resources" during the period.

Special reporting treatments are applied to governmental fund inventories and prepaid expenditures to indicate that they do not represent "current financial resources," since they do not represent net current assets. Such amounts are generally offset by fund balance reserve accounts.

Proprietary, Pension Trust, Private Purpose Trust, and Retiree Health Care Funds are accounted for using the accrual basis of accounting. Their revenues are recognized when they are earned, and their expenses and related liabilities, including claims, judgments, and compensated absences, are recognized when they are incurred. These funds are accounted for on a cost of services or "economic resources" measurement focus. Consequently, all assets and all liabilities (whether current or noncurrent) associated with their activity are included on their balance sheets. The reported Proprietary Fund net assets are segregated into three components: 1) invested in capital assets, net of related debt, 2) restricted net assets, and 3) unrestricted net assets. Proprietary fund type operating statements present increases (revenues) and decreases (expenses) in net assets.

Proprietary funds report both operating and non-operating revenues and expenses in the Statement of Revenues, Expenses, and Changes in Fund Net Assets. The City defines operating revenues as those receipts generated by a specified program offering either a good or service. For example, parking garage and street lot fees are operating revenues of the Parking Fund. This definition is consistent with GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*, which defines operating receipts as cash receipts from customers and other cash receipts that do not result from transactions defined as capital and related financing, non-capital financing or investing activities. Operating expenses include personnel services, contractual services, commodities, other expenses (such as insurance), and depreciation. Revenues and expenses not fitting the above definitions are considered non-operating.

The City's enterprise funds, pension trust, private purpose trust and retiree health care funds and business-type activities, as well as its discretely presented component units, apply all applicable GASB Statements as well as FASB Statements and Interpretations. APB Opinions, and ARBs issued on or before November 30, 1989, in accordance with GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*. The City and its discretely presented major proprietary component units, CPS and SAWS, have elected not to apply any FASB Statements and Interpretations issued after November 30, 1989.

(amounts are expressed in thousands)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

D. Measurement Focus and Basis of Accounting (Continued)

CPS' operating revenue includes receipts from energy sales and miscellaneous revenue related to the electric and gas systems operations. Miscellaneous revenue includes late payment fees, rental income, jobbing and contract work, ancillary services, and merchandise sales. Operating expenses include those expenses that result from the ongoing operations of the electric and gas systems. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses. Non-operating revenues consist primarily of investment income, including the changes in fair value of investments. The amortization of net gains from the lease-back and the sale of water rights in prior years are also included. Some miscellaneous income from renting general property and miscellaneous service is also recorded in non-operating when it is not directly identified with the electric or gas systems.

SAWS' principal operating revenues are charges to customers for water and wastewater services. Operating expenses include the cost of service, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses. Non-operating revenues consist primarily of investment income, including the changes in fair value of investments. Some miscellaneous income from renting general property and miscellaneous service is also recorded in non-operating when it is not directly identified with the water or wastewater services.

E. Future GASB Implementations

GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, establishes accounting and financial reporting standards for the service utility of an asset which has declined significantly and unexpectedly. The provisions of this Statement are effective for fiscal periods beginning after December 15, 2004.

GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, establishes uniform financial reporting standards for other postemployment benefits (OPEB) plans and supersedes the interim guidance included in Statement No. 26. GASB Statement No. 43 follows a similar approach to GASB Statement No. 25 with modifications to reflect differences between pension plans and OPEB plans. The provisions of this Statement are effective for fiscal periods beginning after December 15, 2005.

GASB Statement No. 44, *Economic Condition Reporting: The Statistical Section*, an amendment of NCGA Statement 1, addresses new standards to improve the understandability and usefulness of the information that state and local governments present as supplementary information in the statistical section. The provisions of this Statement are effective for fiscal periods beginning after June 15, 2005.

GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, establishes standards for the measurement, recognition, and display of OPEB expense/expenditures and related liabilities (assets), note disclosures, and, if applicable, required supplementary information (RSI) in the financial reports of state and local governmental employers. The provisions of this Statement are effective for fiscal periods beginning after December 15, 2006.

GASB Statement No. 46, *Net Assets Restricted by Enabling Legislation*, helps governments determine when net assets have been restricted to a particular use by the passage of enabling legislation, and specifies how those net assets should be reported in financial statements when there are changes in the circumstances surrounding such legislation. The provisions of this Statement are effective for fiscal periods beginning after June 15, 2005.

(amounts are expressed in thousands)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

E. Future GASB Implementations (Continued)

GASB Statement No. 47, *Accounting for Termination Benefits*, requires employers to disclose termination benefit arrangements, the cost of the termination benefits, and significant methods and assumptions used to determine termination benefit liabilities. Termination benefits that are provided through an existing defined benefit OPEB plan should be implemented for the fiscal period beginning after December 15, 2006 (simultaneously with GASB Statement No. 45). For all other termination benefits, the provisions of this Statement are effective for periods beginning after June 15, 2005.

The City has not fully determined the effect that implementation of Statements No. 42-47 will have on the City's financial statements.

F. Cash and Cash Equivalents and Investments

The City's investment practices are governed by state statutes and by the City's Investment Policy. City cash is required to be deposited in FDIC-insured banks located within the State of Texas. A pooled cash and investment strategy is utilized which enables the City to have one central depository. Investments are pooled into two primary categories: operating funds and debt service funds. The balances in these funds are invested in an aggregate or pooled amount, with principal and interest income distributed to each respective fund on a pro rata basis. In addition, the City may purchase certain investments with the available balance of a specific fund for the sole benefit of such fund. As of September 30, 2005, the City's investment portfolio did not contain any derivative products nor was it leveraged in any way, except as noted in the Fire and Police Pension Fund. For a listing of authorized investments, see Note 3.

The City, CPS, and SAWS account for and report investments in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. The Fire and Police Pension Plan and the Fire and Police Health Care Fund report investments at fair value in accordance with GASB Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*. The City's policy with respect to money market investments, which had a remaining maturity of one year or less at the time of purchase, is to report those investments at amortized cost, which approximates fair value. Amortization of premium or accretion of discount is recorded over the term of the investments.

For purposes of the statement of cash flows, the City, SAWS, and CPS consider all highly liquid investments with an original maturity of approximately ninety days or less to be cash equivalents.

G. Materials and Supplies and Prepaid Items

Materials and supplies consist principally of expendable items held for consumption and are stated at cost, based on first-in, first-out and lower of average cost or market methods. For governmental and proprietary fund types, the "consumption" method is used to account for materials and supplies. Under the consumption method, these acquisitions are recorded in material and supply accounts and charged as expenditures (governmental fund types) or expenses (proprietary fund types) when used.

Prepaid items are goods and services that are paid for in advance. These payments reflect costs applicable to future accounting periods, and are recorded in both government-wide and fund financial statements. Using the consumption method, prepaid items are charged as expenditures for governmental funds and as expenses for proprietary funds as the goods or services are used.

(amounts are expressed in thousands)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

H. Capital Assets and Depreciation

Primary Government (City)

All capital assets are valued at historical cost or estimated historical cost if actual historical cost is not available. Donated capital assets are valued at their estimated fair value on the date donated. Capital assets recorded under capital leases are recorded at the present value of future minimum lease payments. Depreciation on all exhaustible capital assets of the City is charged as an expense with accumulated depreciation being reported on the Statement of Net Assets. Depreciation is provided over the estimated useful lives of the assets using the straight-line method. With the implementation of GASB Statement No. 34, the City has established capitalization thresholds for infrastructure and machinery and equipment that includes computer equipment. All infrastructure assets are reported in the financial statements, and the estimated useful lives and capitalization thresholds applied are as follows:

Assets	Useful Life	Capitalization
	Years	Threshold
Buildings	15-40	\$ 100
Improvements (Other than buildings)	20-40	100
Machinery and Equipment	2-20	5
Furniture and Office Equipment	5-10	5
Infrastructure	15-100	250

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(amounts are expressed in thousands)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

H. Capital Assets and Depreciation (Continued)

City Public Service (CPS)

The CPS utility plant is stated at the cost of construction, including costs of contracted services, direct equipment, material and labor, indirect costs, including general engineering, labor, equipment, material overheads, and an allowance for funds used during construction (AFUDC). CPS computes AFUDC using rates that approximate the cost of borrowed funds or the short-term investment rate for other funds used for construction. AFUDC is applied to projects estimated to require 30 days or more to complete.

CPS computes depreciation using the straight-line method over the estimated service lives of the depreciable property using specifically identified service lives for each asset type. In 2003, a depreciation study was conducted to determine if existing depreciation rates remained applicable to the depreciable property groups. New rates were applied beginning in 2003. Total depreciation and depletion as a percentage of total depreciable assets net of nuclear fuel was 3.4% for both 2005 and 2004.

CPS amortizes its share of nuclear fuel for the South Texas Project (STP) to fuel expense on a unit-of-production method. Under the Nuclear Waste Policy Act of 1982, the federal government assumed responsibility for the permanent disposal of spent nuclear fuel. CPS is charged a fee for disposal of spent nuclear fuel, which is based upon CPS' share of the STP generation that is available for sale to CPS customers. The charge is included in fuel expense monthly. For further discussion regarding the STP, see Note 10.

The estimated useful lives of capital assets are as follows:

Buildings and structures	15-60 years
Systems and improvements:	
Generation	8-45 years
Transmission and distribution	20-55 years
Gas	50-65 years
Machinery and equipment	4-30 years
Lignite mineral rights and other	20-40 years
Nuclear fuel	1-2 years

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(amounts are expressed in thousands)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

H. Capital Assets and Depreciation (Continued)

San Antonio Water System (SAWS)

The SAWS' capital assets in service are recorded on the unit cost equal to or greater than \$1. Assets acquired through capital leases are recorded on the cost basis and are included in utility plant in service. Assets acquired through contributions, such as those from land developers, are capitalized and recorded in the plant accounts at estimated fair value at date of donation. SAWS capitalizes certain interest costs on revenue bonds and commercial paper associated with newly constructed utility plant additions. Maintenance, repairs, and minor renewals are charged to operating expense, while major plant replacements are capitalized.

SAWS' capital assets are depreciated and property under capital lease is amortized on the straight-line method. This method is applied to all individual assets except distribution mains. Groups of mains are depreciated on the straight-line method using rates estimated to fully depreciate the costs of the asset group over their estimated average useful lives. The table below shows estimated average useful lives used in providing for depreciation of the SAWS' capital assets:

Structures and improvements	50 years
Pumping and purification equipment	10-50 years
Distribution and transmission system	25-50 years
Collection system	50 years
Treatment facilities	25 years
Equipment and machinery	5-20 years
Furniture and fixtures	10 years
Computer equipment	5 years
Software	3 years

I. General Bonded Debt Service

The ad valorem tax rate is allocated each year between the General Fund and the Debt Service Fund. Amounts estimated to be required for debt service on general bonded debt are provided by allocated property taxes, interest earned within the Debt Service Fund, and transfers from other funds.

J. Compensated Absences

In the governmental fund financial statements, the City accrues annual leave and associated employee-related costs when matured (payable from available resources) for City non-uniformed employees and uniformed fire and police employees. In addition, the City accrues the matured portion of the City's uniformed fire and police employees accrued sick leave pay, holiday pay, and bonus pay. Compensatory time is also accrued for the matured portion of the City's non-uniformed, non-exempt employees as well as uniformed police officers.

For governmental fund types, the matured current portion of the liability resulting from the accrual of these compensated absences is recorded in the respective governmental fund and reported in the fund financial statements, while the entire vested liability is reported in the government-wide financials. The current and long-term portions of the liability related to proprietary fund types are accounted for in the respective proprietary fund.

(amounts are expressed in thousands)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

K. Insurance

Activity for the City's self-insurance programs is recorded in the Internal Service Funds. Assets and obligations related to property and casualty liability, employee health benefits, workers' compensation, unemployment compensation, extended sick leave, and employee wellness are included.

The City is insured for property and casualty liability. As of the fiscal year end, Allianz Insurance Company and RSUI Indemnity Company insured the City's property, while the State National Insurance Company provided excess liability coverage. Related liabilities are accrued based on the City's estimates of the aggregate liability for claims made and claims incurred but not reported prior to the end of the fiscal year.

The City also provides employee health, workers' compensation, and unemployment benefits under its self-insured programs. The City is a member of the Texas Municipal League Workers' Compensation Joint Insurance Fund and uses this fund as a mechanism for administering workers' compensation claims for employees that occurred prior to September 30, 1986. Workers' compensation claims that occurred after October 1, 1986 are administered by third-party administrators. In addition, the City has excess workers' compensation coverage through the State National Insurance Company, as of September 30, 2005. The City records all workers' compensation loss contingencies, including claims incurred but not reported.

Employee health benefit liabilities are determined and accrued based upon the City's estimates of aggregate liabilities for unpaid benefits. Regarding unemployment compensation, the City is subject to the State of Texas Employment Commission Act. Under this act, the City's method for providing unemployment compensation is to reimburse the State for claims paid by the State.

All insurance carriers providing coverage for the City are required to possess an A.M. Best Company rating of A- or better, where A- denotes "Excellent." A.M. Best is an industry recognized rating service for insurance companies. For a more detailed explanation of the City's self-insurance programs, see Note 12.

L. Fund Equity

Reservations of fund equity represent amounts that are not appropriate or are legally segregated for a specific purpose. Designations of fund equity represent tentative plans identified by management and are subject to change. Designations are utilized in the City's governmental funds for amounts that have been designated for subsequent years' expenditures and amounts allocated to making future improvements and replacements. Such designations will be reflected on the fund financial statements.

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(amounts are expressed in thousands)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

M. Revenue Recognition

Governmental fund types record revenues on the modified accrual basis of accounting and are reported as such in the fund financial statements. That is, revenues are recorded when they are both measurable and available to finance current operations or when they are considered susceptible to accrual. Revenues from property taxes, sales taxes, municipal court fines and fees, licenses, interest revenue, and charges for services are recorded on the modified accrual basis of accounting, and therefore, are considered susceptible to accrual. The City's availability period is no more than 60 days beyond the end of the fiscal year. When collections are delayed beyond the normal time of receipt due to unusual circumstances, the amounts involved are still recognized as revenues of the current period. "Available" means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Grant revenues are recognized when reimbursable expenditures are made and all other eligibility requirements imposed by the provider have been met. Proprietary-type funds record revenues when earned. In the government-wide financial statements, all revenues are recorded when earned.

CPS revenues are recorded when earned. Customers' meters are read, and bills are rendered monthly. Rate schedules include fuel and gas cost adjustment clauses that permit recovery of fuel and gas costs in the month incurred. CPS reports fuel and distribution gas costs on the same basis as it recognizes revenue. SAWS revenues are recognized when earned under the accrual basis.

N. Allocation of Indirect Expenses

The City recovers indirect costs in the General Fund through the application of departmental indirect cost rates. These rates are developed and documented in the City's departmental indirect cost rate plan. In this plan, each department is classified by function. Indirect costs are budgeted by department and are used as a basis for the City's actual indirect cost allocation. Base rates are then applied to actual indirect costs recovered, and indirect costs are reclassified to reduce general government expenditures. For fiscal year 2005, general government expenditures were reduced by \$7,963, resulting in increased expenditures in other governmental functions and in business-type activities in the amounts of \$4,968 and \$2,995, respectively.

O. Nuclear Decommissioning

CPS, together with the other owners of the STP, filed with the Nuclear Regulatory Commission (NRC) a certificate of financial assurance for the decommissioning of the nuclear power plant. The certificate assures that CPS will meet the minimum decommissioning funding requirements mandated by the NRC. The STP owners agreed in the financial assurance plan that their estimate of decommissioning costs would be reviewed and updated periodically. In 1999, the owners conducted a review of decommissioning costs. The results estimated CPS' share of decommissioning costs at approximately \$311,000 in 1998 dollars. In 2004, the owners conducted an additional review of decommissioning, and results showed that CPS' share of decommissioning costs is now approximately \$397,000 in 2004 dollars.

In 1991, CPS started accumulating the decommissioning funds in an external trust, in accordance with the NRC regulations. The Decommissioning Trust assets and related liabilities are included in CPS' financial statements as a component unit. At December 31, 2004, CPS had accumulated approximately \$222,400 of decommissioning funds in the external trust. Based on the annual calculation of financial assurance required by the NRC, CPS' Decommissioning Trust balance exceeded the calculated financial assurance amount of \$77,300 at December 31, 2004. Based upon the 1998 and 1994 decommissioning cost studies, the annual level funding into the trust of \$6,900 for 2005 was expensed by CPS.

(amounts are expressed in thousands)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

P. Long-Term Obligations

In the government-wide and proprietary fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the statement of net assets. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, governmental fund types recognize bond premiums and discounts as well as bond issuance costs during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts and debt issuance costs are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures of the funds in which proceeds of debt issuances are recorded.

Q. Elimination of Internal Activity

Eliminations of internal activity, particularly those related to internal service fund transactions, are needed to make the transition from governmental funds to government-wide activities. The overriding objective in "eliminating the effects of internal service fund activity" is to adjust the internal charges to cause a break-even result. Eliminating the "effect" of internal service fund activity requires the City to "look back" and adjust the internal service funds' internal charges. Net income derived from internal service fund activity would cause a pro rata reduction in the charges made to the participating funds/functions. Conversely, an internal service fund net loss would require a pro rata increase in the amounts charged to the participating funds/functions. Therefore, eliminations made to the statement of activities remove the "doubling up" effect of internal service fund activity. The residual internal balances between the governmental and business-type activities are reported in the Statement of Net Assets and the internal balance amounts that exist within the governmental funds or within business-type funds are eliminated. The City reports internal service fund balances in both governmental and business-type activities based on the pro rata share of the amounts charged to the participating funds/functions.

The City has three internal service funds: Other Internal Services, Information Technology Services, and Self-Insurance Funds. Other Internal Services and Information Technology Services charges users fees for requested goods or services. Building maintenance charges, a component of the Other Internal Services Fund, are based on the space occupied by departments. Through the tracking of these charges to the applicable departments, the net income or loss will be allocated back to the user department based on actual charges incurred.

The Self-Insurance Funds generate their revenues through fixed assessments charged to the various funds each year. The net income or loss generated by the Self-Insurance Funds is allocated back based on the same allocation by which the revenues are received.

R. Application of Restricted and Unrestricted Net Assets

The City may receive funding from an organization whose expenditure is restricted to certain allowable costs. In situations where both restricted and unrestricted net assets are expended to cover allowable expenses, the City will first expend the restricted net assets and cover additional costs with unrestricted net assets. The City reserves the right to selectively defer the use of restricted assets.

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(amounts are expressed in thousands)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

S. Other Budget Disclosures

Excess of expenditures, transfers, and encumbrances over appropriations occurred as follows:

Excess of Expenditures, Transfers, and Encumbrances Over Appropriations			
Fund/Expenditures	Appropriations	Expenditures, Transfers, and Encumbrances	Excess of Expenditures, Transfers, and Encumbrances over Appropriations
General Fund:			
Health Services	14,245	14,379	134
Economic Development and Opportunity	4,525	4,553	28
Debt Service Fund:	\$ 117,916	\$ 118,810	\$ 894
Special Revenue Funds:			
Stormwater Operations	\$ 22,005	\$ 28,413	\$ 6,408
Job Training, Neighborhood Revitalization and Economic Development	110	159	49
International Center	865	876	11
Capital Improvements Reserve	2,359	4,640	2,281
Nelson Wolff Stadium	667	703	36
Public Health Support Revenue	3,341	4,053	712
Official City Store	425	589	164
Permanent Funds:			
San Jose Burial	\$ 360	\$ 475	\$ 115

With the exception of the Public Health Support Revenue Fund, the excess expenditures over appropriations were fully offset by excess actual revenues or fund balances.

T. Prior Period Adjustments

SAWS' prior year net assets have been restated due to a reclass of 2002 stock dividends in the amount of \$96, settlement payment for a bankruptcy case in the amount of \$7, recording of a prior year payroll expense in the amount of \$26, recording of stock received from Principal Life and MetLife in the amount of \$4,708, and the correction of the capital assets beginning balance in the amount of \$296.

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(amounts are expressed in thousands)

2. PROPERTY TAXES

Property taxes are levied and due upon receipt on October 1, attached as an enforceable lien on property as of January 1, and become delinquent the following February 1. In fiscal year 1999, the City executed an inter-local agreement with the Bexar County Tax Assessor/Collector's Office to provide property tax billing and collection services at the same level of service to its citizens as previously provided by the City.

Property tax revenues are recognized when they become available, which means when due, or past due and receivable within the current period or expected to be collected soon enough thereafter (within 60 days) to be used to pay liabilities of the current period. Property tax receivables, including related interest and penalty receivable, net of allowances for uncollectible amounts, represent amounts the City believes will ultimately be collected. Property tax receivable, net of allowances for uncollectible amounts, are offset by deferred revenues. The City is permitted by the Municipal Finance Law of the State of Texas to levy taxes up to \$2.50 per \$100 of taxable valuation (please note amounts are not reflected in thousands). The tax rate approved by City ordinance for the year ended September 30, 2005, was \$0.57854 per \$100 taxable valuation, which means that the City has a tax margin of \$1.92146 per \$100 taxable valuation (please note amounts are not reflected in thousands). This could raise an additional \$893,133 per year based on the net taxable valuation of \$46,481,975 before the limit is reached.

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(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS

A. Primary Government (City)

City monies are deposited in demand accounts at the City's depository. The City utilizes a pooled cash and investment strategy with each fund's cash balance and pro rata share of highly liquid investments, including U.S. Treasury securities, U.S. government agency securities, and repurchase agreements with original maturities of ninety days or less, summarized by fund type and included in the combined Statement of Net Assets as Cash and Cash Equivalents. Overdrafts which result from a fund overdrawing its share of pooled cash are reported as inter-fund payables by the overdrawn fund and as inter-fund receivables of the General Fund.

Collateral is required for demand deposits and certificates of deposit at 100.0% of all deposits not covered by federal deposit insurance. Obligations that may be pledged as collateral are obligations of the United States and its agencies and obligations of the state and its municipalities, school districts, and district corporations. Collateral pledged for demand accounts and certificates of deposit is required to be held in the City's name in the custody of a third-party institution that customarily provides such custodial services.

Written custodial agreements are required which provide, among other things, that the collateral securities are held separate from the assets of the custodial banks. The City periodically determines that the collateral has a market value adequate to cover the deposits and that the collateral has been segregated either physically or by book entry. At fiscal year-end, cash deposits for the City were entirely collateralized by the City's depository with securities consisting of U.S. government or government agency or U.S. government guaranteed obligations held in book entry form by the Federal Reserve Bank in the City's name.

The City's investment portfolio is managed in accordance with its own Investment Policy and the Texas Public Funds Investment Act, as amended. Authorized investments include: demand accounts, certificates of deposit, obligations of the U.S. Treasury and U.S. government agencies, commercial paper, and repurchase agreements. The City maintains in its investment portfolio U.S. Treasury securities and U.S. government agency securities with original maturities greater than ninety days. Each fund's pro rata share of these investments with original maturities greater than ninety days is combined with similar non-pooled securities (i.e., securities purchased and held for specific funds), including U.S. Treasury securities, and U.S. government agency securities, and are reported as investments in the combined statement of net assets, as of September 30, 2005.

The City accounts for and reports investments in accordance with the GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. The City's policy with respect to money market investments that have a remaining maturity of one year or less at the time of purchase is to report these investments at amortized cost. Amortized cost approximates fair value for these investments. The decrease in fair value for investments of the City with a remaining maturity of greater than one year at the time of purchase was \$167 for the year ended September 30, 2005. The City does not participate in external investment pools.

In accordance with GASB Statement No. 40, *Deposit and Investment Risk Exposure*, the following table and narrative addresses the interest rate risk exposure by investment type using the weighted average maturity (WAM) method, custodial credit risk, credit risk and concentration of credit risk. The City does not hold any foreign securities; therefore, foreign currency risk is not applicable.

A summary of the City's Cash and Cash Equivalents is provided at the conclusion of this note with a comparison to the Statement of Net Assets and Statement of Fiduciary Net Assets.

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(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)

A. Primary Government (City) (Continued)

	City Investments				WAM
	Carrying 1 Amount	Fair 1 Value	Allocation 2	Rating 3	
U.S. Government Agency Securities	\$ 356,935	\$ 356,768	36.4%	AAA	35 years
U.S. Treasuries	379,436	379,436	38.8%	AAA	24 years
Money Market Mutual Fund	58,879	58,879	6.0%	AAA	N/A
Repurchase Agreement	184,053	184,053	18.8%	N/A	N/A
Total City Investments	\$ 979,303	\$ 979,136	100.0%		

1 The Carrying Amount and Fair Value include investments for the Starlight Industrial Development Corporation; Municipal Facilities Corporation, and Convention Center Hotel Finance Corporation which total \$178,960.
2 The allocation is based on Fair Value
3 Standard & Poor's

Custodial Credit Risk (Deposits) – Collateral pledged for demand accounts and certificates of deposit is required to be held in the City's name in the custody of a third party institution that customarily provides such custodial services. The City periodically determines that the collateral has a market value adequate to cover the deposits and that the collateral has been segregated either physically or by book entry. At fiscal year-end, cash deposits for the City were entirely collateralized by the City's depository with securities consisting of U.S. government agency or securities held in book entry form by the Federal Reserve Bank in the City's name.

Custodial Credit Risk (Investments) – The City's investment securities are held at the City's depository bank's third party custodian, the Bank of New York in the City's name.

Interest Rate Risk – The City manages exposure to value losses resulting from rising interest rates by limiting the investment portfolio's weighted-average maturity to five years. Weighted-average maturity is defined as the weighted-average time to the return of a dollar of principal. It is used as an estimate of the interest rate risk of a fixed-income investment. The City invests in a money market mutual funds with 100.0% overnight liquidity. Additionally, the City entered into several repurchase agreements with 100.0% overnight liquidity for investment of certain bond proceeds. A weighted-average maturity in terms of years for the money market mutual funds and the repurchase agreements is not applicable.

Credit Risk – As of September 30, 2005, the City's investment portfolio with the exception of the repurchase agreement and the money market mutual fund investments, consisted only of U.S. Treasury securities and U.S. government agency securities. Investments in U.S. government agency securities including Federal Home Loan Mortgage Corporation, Federal National Mortgage Association, and Federal Home Loan Bank were rated Aaa by Moody's Investors Services and AAA by Standard & Poor's. The investments in the money market funds were rated Aaa by Moody's Investor Service and AAA by Standard & Poor's, and all repurchase agreements were over 100% collateralized with U.S. government agency securities. The City manages its exposure to credit risk by limiting its fixed income investments to a rating of "A" or better.

Concentration of Credit Risk – Although the City's Investment Policy does not limit the amount of the portfolio invested in any one U.S. government agency, the City manages exposure to credit risk through diversification. As of September 30, 2005 the U.S. government agency securities allocation was as follows: Federal Home Loan Mortgage Corporation 18.6%, Federal National Mortgage Association 16.2%, and Federal Home Loan Bank 1.6 %.

(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)

B. Fire and Police Pension Fund

Investments of the Fire and Police Pension Fund (Pension Fund), a blended component unit, are administered by the Fire and Police Pension Fund Board of Trustees. Investments of the Pension Fund are reported at fair value and include: corporate bonds; common stock; preferred stock; U.S. Treasury securities; U.S. government agency securities; notes, mortgages, hedge funds and contracts; and real estate. Equity and fixed income securities traded on national or international exchanges are valued at the last reported sales price at current exchange rates. Notes, mortgages and contracts are valued on the basis of future principal and interest payments discounted at prevailing interest rates. The fair value of real estate investments is based on independent appraisals and on the equity position of real estate partnerships in which the Pension Fund has invested. Investment income is recognized as earned. Gains and losses on sales and exchanges are recognized on the trade date. Investments that do not have an established market are reported at estimated fair value. The Pension Fund's assets are invested as authorized by Texas state law. As of September 2005, the Pension Fund had the following investments:

	2005
Cash and short-term investments	\$ 98,847
Securities lending collateral-cash and cash equivalents:	
U.S. government agencies	
Corporate Bonds	11,214
Common Stock	18,909
U.S. Treasury Bonds	90,244
GLOBAL equities	28,264
Corporate Bonds	13,881
Government and agency issues	78,780
Preferred Stock	201,868
Common Stock	622
Hedge Funds	853,687
Notes, mortgages, and contracts	161,968
Venture capital, partnerships, and other alternative investments	81,912
Real Estate	106,690
Total	1,864,848

Custodial Credit Risk (Deposits). Cash and short term investments include demand deposits accounts, equity in pooled cash of the City, and short-term U.S. government and other investments. As of September 30, 2005, cash in demand deposit accounts and the pooled cash of the City were fully collateralized.

Custodial Credit Risk-(Investments). For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Pension Fund will not be able to recover the value of its investments or collateral securities that are in the possession of the outside party. As of September 30, 2005, the Pension Fund had investment in foreign currency in the amount of \$338 that were uninsured and uncollateralized.

Credit Risk. Using Standard and Poor's rating system for fixed-income securities as of September 30, 2005, 73.0% of the Pension Fund's bonds were rated AAA, 0.8% were rated AA, 6.6% were rated A, 3.5% were rated BBB, 3.7% were rated BB, 8.2% were rated B, 1.8% were rated below B, and 2.4% were not rated.

(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)

C. Fire and Police Pension Fund (Continued)

Interest Rate Risk. Only the fixed-income securities of the Pension Fund are subject to interest rate risk due to the possibility that prevailing interest rates could change before the securities reach maturity. Total interest rate sensitive securities amount to \$267,130 and have a Weighted Average Maturity of 7.73 years. Securities that are subject to Interest Rate Risk are shown in the following table:

Investment Type	Fair Value	Weighted Average Maturity (Years)
Corporate Bonds	\$ 72,710	7.54
Government Agencies	56,680	9.72
Government Bonds	54,935	5.99
Short Term Bills and Notes	26,689	0.23
Asset-Backed Securities	20,964	8.96
Government Mortgage-Backed Securities	17,146	16.68
Municipal/Provincial Bonds	10,736	4.8
Corporate Convertible Bonds	4,269	9.49
Non-Government Backed C.M.O.s	2,420	17.43
Commercial Mortgage-Backed	581	37.78
Total Interest Rate Sensitive Securities	\$ 267,130	
Portfolio Weighted Average Maturity		7.73

Foreign Currency Risk. The Pension Fund's investments include investments in stocks and bonds in foreign currency denominations. Stocks denominated in foreign currencies as of September 30, 2005 amounted to \$752 in cash and \$77,679 in common stock. Bonds denominated in foreign currencies amounted to \$65,031.

Stocks denominated in foreign currencies as of September 30, 2005 are as follows:

	Cash	Common Stock
Australian dollar	\$ 46	\$ 3,470
Swiss franc	18	5,159
Danish krone		939
Euro	287	26,808
British pound sterling	145	18,705
Hong Kong dollar	25	1,247
Japanese yen	106	18,192
Norwegian krone	1	861
Swedish krona	112	1,848
Singapore dollar	12	450
	\$ 752	\$ 77,679

(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)

B. Fire and Police Pension Fund (Continued)

Bonds denominated in foreign currencies are as follows:

Investment	Currency	Maturity	Fair Values
New South Wales TSY	Australian Dollar	05/01/12	\$ 4,064
New South Wales TSY	Australian Dollar	12/01/10	4,329
Queensland TSY CP	Australian Dollar	09/14/07	4,284
UK Treasury	British Pound Sterling	09/07/15	4,634
Canada Government	Canadian Dollar	06/01/11	5,257
Canada T-Bills	Canadian Dollar	01/26/06	10,647
Linsey Modern	Canadian Dollar	06/18/08	156
Rogers Cantel Mobi	Canadian Dollar	06/01/06	228
Germany (Fed Rep)	Euro	07/04/10	3,949
Germany (Fed Rep)	Euro	07/04/09	4,627
Germany (Fed Rep)	Euro	07/04/09	4,125
Ontario Provincial	New Zealand Dollar	06/16/15	2,139
New Zealand (Govt)	New Zealand Dollar	04/15/15	2,125
Poland (Rep Of)	Polish Zloty	06/24/08	8,336
Singapore Govt	Singapore Dollar	10/15/05	2,058
Singapore Govt	Singapore Dollar	03/01/07	1,756
Singapore Govt	Singapore Dollar	10/01/07	2,317
			<u>\$ 65,031</u>

Guaranteed Contract - One investment, a contract with Pacific Life Insurance Company, guarantees a return of the Lehman Brothers Aggregate Bond Index plus 15 basis points. The market value of this investment as of September 30, 2005, was \$81,912, which is approximately 5.0% of the invested assets of the fund at September 30, 2005. This investment, although not directly invested in bonds, is also sensitive to changes in interest rates and credit risk. The sensitivity and risk would be approximately the same as the index. As of September 30, 2005, the index had a weighted average maturity of seven years. 78.1% of the index is rated AAA, 4.9% of the index is rated AA, 8.8% is rated A and 8.3% is rated BBB.

Securities Lending - State statutes and Pension Fund policies allow for securities lending transactions. The Pension Fund has entered into an agreement with its custodial bank to lend the Pension Fund's securities to one or more borrowers for a fee. It is the policy of the Pension Fund and the custodial bank to require that collateral equal to 102.0% and 105.0% for domestic and international securities, respectively, of the loaned securities are maintained by the custodial bank. Collateral may be in the form of cash, U.S. government securities and irrevocable letters of credit. Until such time as the loan is terminated, the borrower retains all incidents of ownership with respect to the collateral. In the event that the borrower fails to repay the borrowed securities when due, and the value of the collateral is insufficient to replace the borrowed securities, the Pension Fund may suffer a loss. Management of the Pension Fund considers the possibility of such a loss to be remote. Cash open collateral is invested in a short-term investment pool with an average weighted maturity of 27 days at September 30, 2005.

(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)

A. Fire and Police Pension Fund (Continued)

As of September 30, 2005, the Pension Fund had lending arrangements outstanding with a total market value of \$165,158 which were fully collateralized, with cash and securities. Of this amount, cash collateral of \$162,512 is recorded in the accompanying Statements of Plan Fiduciary Net Assets. Net income for the year ended September 30, 2005 under the securities lending arrangement was \$360.

The Pension Fund has only limited involvement with derivative and other structured financial instruments (as defined in GASB Technical Bulletin No. 94-1) and does not use them for trading purposes. The Pension Fund's investment philosophy in bond portfolios has centered on using derivatives and other structured financial instruments only when comparable cash alternatives are not available. Specifically, the Pension Fund has used the following basic guidelines when entering into such transactions: (1) small allocations, (2) no use of leverage, (3) price floors, (4) short maturities to mitigate potential problems with liquidity, and (5) attention to credit risk of the issuer. The fair value of structured financial instruments held for the Pension Fund at September 30, 2005, was approximately \$2,420.

A summary of the Pension Fund's Cash and Cash Equivalents is provided at the conclusion of this note with a comparison to the Statement of Fiduciary Net Assets

C. Fire and Police Retiree Health Care Fund

The Health Care Fund periodically participates in options and futures to hedge the value of a portion of its investments. Financial options and futures are agreements that give one party the right, but not the obligation, to buy or sell a specific amount of an asset for a specified price on or before a specified expiration date. However, at September 30, 2005, there was no exposure to options or futures.

The Fire and Police Retiree Health Care Fund (Health Care Fund) Board of Trustees administers investments of the Fire and Police Retiree Health Care Fund, a blended component unit. Investments are reported at fair value, and short-term investments are reported at amortized cost, which approximates fair value. Securities traded on national or international exchanges are valued at the last reported sales price at current exchange rates. Investments in Hedge Fund or Funds, real estate investment trusts and alternative investments are held in the form of Limited Partnership investments. The fair valuation of these investments is set by the Limited Partnerships and/or by independent appraisers.

The Health Care Fund's assets are invested as authorized by the Investment Policy Statement and Guidelines of the San Antonio Fire and Police Retiree Health Care Fund, San Antonio (Investment Policy). The Health Care Fund utilizes an investment consultant to make recommendations as to the appropriate target portfolio weightings among the major assets classes (e.g. stocks, bonds, cash) within the fund. Additionally, the Health Care Fund has hired certain investment managers to exercise full discretionary authority as to all buy, hold and sell decisions for each security under management, subject to the guidelines as defined in the Investment Policy. All of the Health Care Fund's assets are held by a custodian bank, Frost National Bank of San Antonio, Texas.

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(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)

C. Fire and Police Retiree Health Care Fund (Continued)

Investments authorized by the Health Care Fund's Investment Policy include U.S. equities, including common stocks, securities convertible into common stock, and open or closed-end mutual funds; international equity; certain fixed-income assets and alternative investments, including real estate, absolute return hedge funds and timber. The cash portion of the Health Care Fund will be invested in a short-term investment fund administered by the custodian bank, a Money Market Mutual Fund, or in individual permissible securities. The fair value of the Health Care Fund's cash and investments at September 30, 2005 is \$164,808.

Cash	\$	535
Securities lending collateral-cash and cash equivalents		15,200
Cash equivalents and money market funds		11,325
U.S. Government and agency issues		3,545
Corporate Bonds		6,848
Common Stock		67,826
Bond mutual funds		10,665
Real estate investment trusts (REIT)		12,057
Mutual funds-Invest in Common stock		18,987
Hedge Fund of Funds		12,935
Alternative Investments		4,885
Total	\$	164,808

Custodial Credit Risk (Deposits) – The Health Care Fund's deposits held with the custodian bank are insured up to \$100 by federal deposit insurance. Deposit balances over \$100 are not insured and are uncollateralized. There are no state regulations, however, which require the fund to maintain collateral for demand deposits not covered by federal deposit insurance. The bank balance of the Health Care Fund, which is exposed to custodial credit risk as of September 30, 2005, is \$712. The Health Care Fund does not have deposit or investment policies related to custodial credit risk as of September 30, 2005. The Health Care Fund is aware of these risks and monitors such risks as part of its day-to-day operations and through its daily dealings with the custodian bank.

Custodial Credit Risk (Investments) – The Health Care Fund's investment securities, stocks, and bonds, are held at Frost National Bank's third-party custodian, Bank of New York. All securities held for the Health Care Fund at the Bank of New York are in Frost Bank's name, and Frost Bank tracks these securities as being held for the benefit of the Health Care Fund. Since the securities are not registered in the name of the Health Care Fund, are held by a counterparty, and are not insured, they are considered to be exposed to custodial credit risk. These investments are reported as follows, by investment type, as of September 30, 2005:

Government Bonds	\$	3,545
Corporate Bonds		6,848
Common Stock		67,826
Mutual Fund		18,987
Money Market Mutual Fund		11,325

Credit Risk – According to the Investment Policy of the Health Care Fund the average credit quality rating for the fixed-income portfolio will be at least "A." Ninety percent of the securities must be rated BBB-/Baa3 or higher by a nationally recognized rating agency at time of purchase. For split-rated securities, the higher rating will be used in determining compliance with these guidelines. Credit quality ratings for investments with credit risk were AAA/Aaa for the Money Market Mutual Fund, AA- for Corporate Bonds, AAA for Bond Mutual Funds and U.S. Government and Agency Issues are not provided or required to have their rating disclosed.

(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)

C. Fire and Police Retiree Health Care Fund (Continued)

Concentration of Credit Risk – The Health Care Fund's Investment Policy regarding concentration of credit risk for equities states that no more than 5.0% of any investment manager's portfolio at cost and 8.0% at the market value shall be invested in the securities of any one company. Regarding fixed-income assets, no more than 10.0% of an investment manager's bond portfolio at cost shall be invested in the securities of any one issuer. The policy further states there shall be no such limit on U.S. government securities, U.S. agency securities or government sponsored entities, U.S. agency mortgage-backed securities, or other sovereign issues rated "AAA" or "Aaa." At year-end, the Health Care Fund did not have any investments in any one issuer that represented 5.0% or more of total investments.

Interest Rate Risk – The Health Care Fund does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. The Health Care Fund is aware of this risk and has chosen to rely on the expert advice of professional money managers to manage its exposure to interest rate changes. The Weighted Average Maturity at September 30, 2005 is 7.99 years for Corporate Bonds, 24.62 years for U.S. Government and Agency issues and 6 years for Bond mutual funds. The respective fair value of each investment type is \$6,848, \$3,545 and \$10,665. The Money Market Mutual Fund had a fair value of \$11,324 at year-end and is payable on demand.

As of September 30, 2005, the Health Care Fund held a Collateralized Mortgage Obligation (CMO) position and mortgage-backed securities in the form of Government National Mortgage Association (GNMA), Federal National Mortgage Association (FNMA), Federal Home Loan Mortgage Corporation (FHLMC), and similar pass-through obligations. Because mortgage borrowers have the option of prepaying their mortgages, asset-backed securities such as mortgage pass-through securities issued by GNMA, FNMA, and FHLMC are considered to be highly sensitive investments. The overall return or yield on CMOs and asset-backed securities depends on the amount of interest collected over the life of the security and the change in the market value. Although the Health Care Fund will receive the full amount of principal, if prepaid, the interest income that would have been collected during the remaining period to maturity, net of any market adjustment, is lost. The fair value of the CMO and mortgage-backed securities held by the Fund was approximately \$3,545 as of September 30, 2005.

Securities Lending – Securities Lending assets are reported at fair value. Investment Policy of the Health Care Fund and state statutes allow for securities lending transactions. The Health Care Fund entered into an agreement with its custodian bank in June 2003 to lend the Fund's securities to one or more borrowers for a fee. It is the policy of the Health Care Fund and the custodian bank to require that collateral equal 100.0% of the loaned security's market value plus accrued interest for domestic government or agency securities loaned and 102.0% of the loaned security's market value plus accrued interest for approved, domestic non-government or agency securities loaned be maintained by the custodian bank. Collateral may be in the form of cash, U.S. government securities, or irrevocable letters of credit. Until the loan is terminated, the borrower retains all incidents of ownership with respect to the collateral. If the borrower fails to repay the borrowed securities when due and the value of the collateral is insufficient to replace the borrowed securities, the Health Care Fund may suffer a loss. Management of the Health Care Fund considers the possibility of such a loss to be remote. Cash collateral is invested in money market funds at September 30, 2005.

A summary of the Retiree Health Care Funds Cash and Cash equivalents is provided at the conclusion of this note with a comparison to the Statement of Fiduciary Funds.

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(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)

D. City Public Service (CPS)

The investment policy of CPS, a major discretely presented component unit, is governed by state statute, local ordinance, and CPS Board Resolution and Policy. CPS' allowable investments include U.S. government or government agency or U.S. government guaranteed obligations, collateralized mortgage obligations issued by the U.S., fully secured certificates of deposit issued by a state, national bank, or savings bank domiciled in the State of Texas, direct repurchase agreements, reverse repurchase agreements, defined bankers acceptances and commercial paper, no-load money market mutual funds, and other types of specific secured or guaranteed investments.

CPS cash deposits at January 31, 2005, were entirely insured by federal depository insurance or collateralized by banks for the account of CPS. For deposits that were collateralized, the securities were U.S. government or government agency or U.S. government guaranteed obligations held in book entry form by the Federal Reserve Bank in CPS' name.

CPS' investments with a maturity date within one year of the purchase date are reported at amortized cost, which approximates fair value. Amortization of premium and accretion of discount are recorded over the terms of the investments that mature within one year. CPS investments with a maturity date of one year or longer from the purchase date are accounted for using fair value. Fair value is determined by using generally accepted financial reporting services and publications and approved dealers and brokers as necessary. The specific identification method is used to determine costs in computing gain or loss on sales of securities.

CPS' cash, cash equivalents, and investments can be separated by those that are directly managed by CPS, those managed through the Decommissioning Trust and those managed through the Employee Benefit Plans. For financial reporting purposes, cash, cash equivalents and investments managed directly by CPS have been consistently measured as the end of the applicable fiscal years as well as the results of the Decommissioning Trust and the Employee Benefit Plans. For fiscal year 2005, consolidation practices were modified whereby the results of the Decommissioning Trust and the Employee Benefit Plans were included as of their separately audited calendar year ends.

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(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)

D. City Public Service (CPS) (Continued)

The following is a summary of CPS total Investments by types as well as detailed risk analysis and disclosures in accordance with GASB statement No 40. *Deposit and Investment Risk Disclosures*.

Summary of Investments by Type Fiscal Year Ending January 31, 2005	
Total Investments By Category	2005
CPS Investments:	
U.S. Treasuries, Government Agency Security & Money Market Funds	\$ 1,020,104
Decommissioning Trust:	
U.S. Treasuries, Government Agency Securities & Money Market Funds	\$ 220,526
Employee Benefit Plans	
Money Market Mutual Fund	20,442
Corporate Bonds	20,401
Common Stock	102,575
U.S. Treasury & Government Agency Securities	24,412
Global bonds	9,147
Total Employee Benefit Plans	\$ 176,977
Grand Total - All Investments	\$ 1,417,607

Cash equivalents and investments are exposed to interest rate risk, credit risk (including custodial credit risk and concentrations of credit risk), and foreign currency risk. Interest risk is the exposure to fair value losses arising from rising interest rates. Credit risk is the risk that an issuer of an investment will not fulfill its obligations (will be unable to make timely principal and interest payments on the security). Foreign currency risk is the exposure to fair value losses arising from changes in exchange rates. Cash, cash equivalents, and fixed-income investments are also exposed to inflation, liquidity, political, legal, event, reinvestment, and timing (call) risk. Additionally, equity investments are exposed to political, legal, event and general economic risk. CPS identifies and manages all of these risks by following an appropriate investment oversight strategy, establishing and monitoring compliance with investment policies and procedures, and continual monitoring of prudent risk controls. All investments follow the "prudent person" concept.

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(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)

D. City Public Service (CPS) (Continued)

CPS Direct Investments

In accordance with CPS' year end adoption of GASB Statement No. 40 the following table and narrative addresses interest rate risk exposure by investment type using the weighted average maturity (WAM) method, credit risk, and concentration of credit risk. Since CPS does not hold foreign instruments in its direct investments foreign currency risk is not applicable.

	CPS Direct Investments			
	Carrying Amount	Fair Value	Allocation	Rating
U.S. Government Agency Securities	\$ 967,955	\$ 967,885	94.9%	AAA
U.S. Treasuries	7,980	7,980	0.8%	AAA
Money Market Mutual Fund	44,169	44,169	4.3%	AAA
Total CPS Direct Investments	\$ 1,020,104	\$ 1,020,034	100.0%	N/A

Interest Rate Risk - CPS manages exposure to fair value losses resulting from rising interest rates by limiting the portfolios weighted-average maturity to two years. Weighted-average maturity is defined as the weighted-average time to the return of a dollar of principal. It is used as an estimate of the interest rate risk of a fixed-income investment. CPS invests in money market mutual funds that have no fixed maturities. Accordingly, a weighted-average maturity in terms of years for money-market funds is not applicable.

Credit Risk - CPS manages exposure to credit risk by limiting its fixed income investments to a rating of "A" or better. As of January 31, 2005, CPS held no direct investments with a rating below AAA.

Concentration of Credit Risk - CPS manages exposure to credit risk through diversification and by limiting its investment in each government-sponsored entity to 50.0% and its investment in any other non-government issuer to 5.0% of the total fixed income portfolio. Investments in U.S. Government Agencies were allocated as follows: Federal Farm Credit Banks (FFCB) 3.8%; Federal Home Loan Bank (FHLB) 36.0%; Federal Home Loan Mortgage Corporation (FHLMC) 23.5%; and Federal National Mortgage Association (FNMA) 31.6%.

Decommissioning Trust - CPS' investments in the Decommissioning Trust are held by an independent trustee. Trust investments are limited to U.S. government or government agency or U.S. government guaranteed obligations by CPS Board Resolution and Policy, Trust Agreement, and State law. These investments are subject to market risk, and their fair value will vary as interest rates fluctuate. This could affect the value at which these securities are recorded. Decommissioning Trust investments are reported at fair value.

The following table and narrative addresses interest rate risk exposure by investment type using the weighted average maturity (WAM) method, credit risk, and concentration of credit risk. Since the Decommissioning Trust does not hold foreign instruments, foreign currency risk is not applicable.

	Decommissioning Trust Investments			
	Carrying Amount	Fair Value	Allocation	Rating
U.S. Government Agency Securities	\$ 206,088	\$ 206,088	93.5%	AAA
U.S. Treasuries	8,935	8,935	4.1%	AAA
Money Market Mutual Fund	5,503	5,503	2.4%	AAA
Total Decommissioning Trust	\$ 220,526	\$ 220,526	100.0%	N/A

(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)

D. City Public Service (CPS) (Continued)

Interest Rate Risk - The Trust manages exposure to fair value losses resulting from rising interest rates by ensuring the total portfolio's weighted-average maturities do not extend beyond the final decommissioning, which is currently scheduled for 2047. The Decommissioning Trust invests in money market mutual funds that have no fixed-income maturities. Accordingly, a weighted-average maturity in terms of years for money market funds is not applicable.

Credit Risk - The Trust manages its exposure to credit risk by limiting its fixed-income investments to a rating of "A" or better. As of this plan's year-end, the Trust held no investments with a rating below AAA.

Concentration of Credit Risk - The Trust manages exposure to credit risk through diversification and by limiting its investment in each government-sponsored entity to 50.0% and its investment in any other non-government issuer to 5.0% of the total fixed income portfolio. Investments in U.S. government agencies were allocated as follows: FFCB 16.7%; FHLB 43.8%; FHLMC 6.2%; and FNMA 26.8%.

CPS Employee Benefit Plans - Investments in the Employee Benefit Plans are also held by an independent trustee. These investments are limited to those authorized by the plans' Administrative Committees, the Trust Agreements, and State law. These investments are subject to market risk and their fair value will vary as interest rates fluctuate. This could affect the value at which these securities are recorded. These investment policies follow the "prudent person" concept. CPS reports Employee Benefit Plan investments at fair value.

CPS employee benefit plans consist of three separate plans. The plans include the City Public Service of San Antonio Group Health Plan (the "Health Plan"), the Disability Income Plan (the "Disability Plan") and the Life Insurance Plan (the "Life Plan"). The following tables and narrative address interest rate risk exposure by investment type using the weighted average maturity (WAM) method, credit risk, and concentration of credit risk.

	Weighted Average Maturity of Investments					
	Health Plan		Disability Plan		Life Plan	
	Fair Value	WAM	Fair Value	WAM	Fair Value	WAM
U.S. Treasuries and Government Agency Notes and Bonds	\$ 6,190	6.5 years	\$ 491	5.6 years	\$ 2,417	6.1 years
STRIPS					190	24.7 years
Collateralized Mortgage Obligations	4,191	6.0 years	110	5.2 years	2,786	5.1 years
Mortgage Pass-through Securities	4,295	2.9 years	140	2.3 years	2,096	2.5 years
Total U.S. Government Agency Securities	\$ 14,676		\$ 741		\$ 7,489	
Commercial Mortgage-backed Securities	\$ 1,347	7.2 years	\$ 79	8.4 years	\$ 375	8.9 years
Asset-backed Securities	2,259	3.9 years	140	.5 years	1,269	5.4 years
Corporate Bonds	12,572	2 years	327	3.8 years	3,540	4.3 years
Foreign Bond Fund	6,679	NA			2,468	5.3 years
Money Market Mutual Funds	16,779		593	NA	3,180	NA
Total Employee Benefit Plans	\$ 54,312	3.4 years	\$ 1,880	3.0 years	\$ 18,321	6.4 years

Interest Rate Risk - The table above reflects each Employee Benefit Plans' weighted average maturity (WAM) of the fixed-income classes. In accordance with its historical guidelines and investment policy the Administrative Committee manages exposure to fair value losses arising from rising interest rates by limiting the average maturity date of each manager's portfolio to no more than ten years. Each Employee Benefit Plan invests in money market mutual funds that have no fixed maturities. Accordingly, a weighted average maturity in terms of years for money market mutual funds is not applicable.

(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)

D. City Public Service (CPS) (Continued)

Credit Rating	Investments Allocated by Credit Rating					
	Health Plan		Disability Plan		Life Plan	
	Fair Value	Allocation	Fair Value	Allocation	Fair Value	Allocation
Government	\$ 2,209	4.1%	\$ 226	12.0%	\$ 918	5.0%
AAA	32,508	59.9%	1,327	70.6%	11,528	62.9%
AA	1,208	2.2%	55	2.9%	772	4.2%
A	5,074	9.3%	168	8.9%	2,295	12.5%
BBB	658	1.2%	104	5.6%	340	1.9%
Less than BBB	5,976	11.0%				
Navarro Investments, L.L.C.	6,679	12.3%			2,468	13.5%
Total Employee Benefit Plans	\$ 54,312	100.0%	\$ 1,880	100.0%	\$ 18,321	100.0%

Credit Risk - The table above presents the Employee Benefits Plans' percentage of fixed-income investments allocated by credit rating. In accordance with its historical guidelines and investment policy, the Administrative Committee manages exposure to credit risk by limiting investments rated below BBB to 7.5% of total fixed income investments. Excluding Navarro Investments, L.L.C. that were not evaluated as a fund by a rating agency, at December 31, 2004, investments with a rating below a BBB rating amounted to 11.0%. Policy constraints on less than BBB rated bonds will be reviewed in light of enhanced yields obtained during periods of low interest rates. Even though the Health Plan holds approximately 12.3% and the Life Plan holds approximately 13.5% of the fixed-income investments in funds that are not rated by a rating agency, the majority of the underlying securities are rated. Weighing the securities by market value (U.S. Dollars) and evaluating the corresponding rating of the underlying securities indicate that 1.9% of the investments are unrated or have a rating of less than BBB.

Top Issuers	Fair Value of Issuer 5.0% or Greater					
	Health Plan		Disability Plan		Life Plan	
	Fair Value	Allocation	Fair Value	Allocation	Fair Value	Allocation
AIM Short-Term Investment	\$ 16,669	30.7%	\$ 593	31.5%	\$ 3,180	17.4%
FNMA	7,207	13.3%	202	10.8%	3,251	17.7%
Navarro Investments L.L.C.	6,679	12.3%			2,468	13.5%
FHLMC	4,327	8.0%	211	11.2%	2,081	11.4%

Concentration of Credit Risk - The table above presents the Employee Benefit Plans' fair values of investments by issuer representing 5.0% or more of the fixed-income investments. In accordance with historical guidelines and investment policy, the Administrative Committee has established maximum holdings of other than federal government issuers so that in the event of failure of any one issuer it would not affect the entire investment portfolio. Further, the Committee manages exposure to credit risk through diversification and by limiting the amount, which may be invested in any one corporate bond issuer to 10.0% of the corporate bond investment portfolio of each investment manager. There is no limit, which may be invested in U.S. Treasury securities, government-guaranteed, or government sponsored entity securities, other than the maximum of 50.0% in any one government-sponsored entity issuer.

(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)

D. City Public Service (CPS) (Continued)

Foreign Currency Risk - The Health Plan and the Life Plan have \$6,679 and \$2,468, respectively, invested in the Navarro Investments L.L.C Foreign Bond Fund at December 31, 2004. The historical guidelines and new investment policy place a 6.5% of total investment portfolio limit on the amount, which may be invested, in foreign currency-denominated securities. The foreign currency risk is further mitigated by the investment guidelines in the fund.

A summary of the CPS Cash and Cash Equivalents is provided at the conclusion of this note with a comparison to the Statement of Net Assets.

E. San Antonio Water System (SAWS)

The investment policy of SAWS, a major discretely presented component unit, is governed by state statute, local ordinance, and their own respective written investment policy. SAWS is permitted by City Ordinance No. 75686 to invest in direct obligations of the United States or its agencies and instrumentalities. Other allowable investments include direct obligations of the State of Texas or its agencies and instrumentalities; secured certificates of deposit issued by state and national banks domiciled in the State of Texas; defined bankers' acceptances and commercial paper; collateralized direct repurchase agreements; reverse repurchase agreements; no-load money market mutual funds; investment pools; and other types of secured or guaranteed investments. These investments are subject to market risk, interest rate risk, and credit risk and affect the value at which these investments are recorded.

Under the provisions of GASB Statement No. 31, SAWS reports money market investments with a remaining maturity at time of purchase of one year or less at amortized cost, which approximates fair values. The net decrease during fiscal year 2004 in the fair value of the money market investments with an original maturity of greater than one year was \$1,400. This amount takes into account all changes in fair value (including purchases and sales) that occurred during the year. The unrealized gain on investments held at year-end was \$357.

Credit Risk (Deposit) - All funds are deposited at JP Morgan/Chase Bank One N.A., SAWS' general depository bank. The general depository agreement does not require that SAWS maintain an average monthly balance. As required by state law, all deposits are fully collateralized and/or are covered by federal depository insurance. The collateral pledged is being held by the Federal Reserve Bank of New York under SAWS' name on December 31, 2004. As of December 31, 2004, the bank balance of demand and savings account was \$9,583, and the reported amount was \$7,404, which includes \$191 of cash on hand.

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(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)

E. San Antonio Water System (SAWS) (Continued)

Credit Risk (Investment) - All investments, with the exception of those held in escrow, are in securities of the U.S. Treasury or Agencies of the United States and are held in safekeeping by the general depository bank, registered as accounts of SAWS. Funds held in escrow, are money market funds managed by Wachovia Bank and JP Morgan Chase/Bank One and are invested in U.S. Treasury obligations.

As of December 31, 2004, SAWS had the following investments and maturities:

Investment Type	Fair Value	Investment Maturities (in Days)					Reported Amount
		Less than 90	91 to 180	181 to 365	Greater Than 365		
U.S. Treasury Bills	\$ 27,876	\$ 6,396	\$ 13,295	\$ 8,185		\$	\$ 27,892
U.S. Treasury Notes	69,735		5,540	50,836	13,359		69,853
U.S. Agency Discount Notes	91,994		4,874	87,120			92,125
U.S. Agency Coupon Notes	93,796		2,936	23,273	67,587		93,872
Money Market Funds:							
Wachovia Bank	7,877	7,877					7,877
JP Morgan Chase/Bank One	2,926	2,926					2,926
	\$ 294,204	\$ 17,199	\$ 26,645	\$ 169,414	\$ 80,946	\$	\$ 294,545
Percentage of Portfolio	100%	6%	9%	58%	27%		

Interest Rate Risk - As a means of limiting its exposure to fair value losses due to rising interest rates, SAWS investment policy limits its investment maturities to no more than five years. As indicated in the table above, more than half (73.0%) of SAWS' investment portfolio is invested in maturities less than one year.

Credit Risk - SAWS manages its exposure to credit risk by limiting its fixed-income investments to a rating of "A" or better. Investments in government sponsored entities such as Federal Home Loan Bank, Federal National Mortgage Association, Federal Home Loan Mortgage Corporation, and Federal Farm Credit Bank were rated Aaa by Moody's Investor Service and AAA by Standard & Poor's and Fitch's Ratings. The investments in money market funds were rated Aaa by Moody's Investor Service and AAA by Standard and Poor's.

Concentration of Credit Risk - There are no restrictions in SAWS' investment policy on the amount it may invest in any one issuer. Therefore, SAWS has invested more than five percent of its investments in government sponsored entities, in the form of discount or coupon notes. The percentage invested in each issuer as a percent of the total portfolio is as follows: 13.6% in the Federal Home Loan Bank, 10.0% in the Federal National Mortgage Association, and 37.8% in the Federal Home Loan Mortgage Corporation.

Pay-Fixed, Receive-Variable Interest Rate Swap - Objective of the Interest Rate Swap: On March 27, 2003, SAWS entered into an interest rate swap agreement in connection with its City of San Antonio, Texas Water System subordinate Lien Revenue and Refunding Bonds, Series 2003-A and 2003-B (the Series 2003 Bonds) issued in a variable interest rate mode. The Series 2003 bonds were issued to provide funds for the Capital Improvement program and to refund certain outstanding commercial paper notes. The swap was used to hedge interest rates on the series 2003 Bonds to a synthetic fixed rate that produced a lower expected interest rate cost to the SAWS than traditional long term fixed rate bonds.

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(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)

E. San Antonio Water System (SAWS) (Continued)

Terms, Fair Values, and Credit Risk - The terms, including the counterparty credit ratings of the outstanding swap, as of December 31, 2004, are included in the table below. The System's swap agreement contains scheduled reductions to the outstanding notional amounts that are expected to follow scheduled reductions in the associated bonds. The Series 2003 Bonds were issued on March 27, 2003, with a principal amount of \$122,500. The swap was structured to match the principal amortization structure and dates of the Series 2003 Bonds. The counterparty to the swap is Bear Stearns Financial Products, Inc. ("Bear Stearns").

Related Bonds	Maturity	Counterparty	CP Rating by		Variable Rate	Fixed Rate		Market Value
			Moody's/S&P	Fitch	Received	Paid		
Series 2003	May 1, 2003	Bear Stearns	Aaa/AAA/AAA		BMA	4.18%	\$	(3,125)

The combination of variable rate bonds and a floating-to-fixed swap create a synthetic fixed-rate issue for the SAWS. The synthetic fixed-rate protects against the potential of rising interest rates in conjunction with the SAWS Series 2003 Bonds issues in a weekly mode and achieves a lower fixed rate than in the traditional fixed rate bond market at the time of issuance.

Fair Value - The swap had a negative fair value as of December 31, 2004 of \$(3,125). This value was calculated using the zero-coupon method. This method calculates the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipated future spot interest rates. These net payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement on the swap.

Credit Risk - As of December 31, 2004, SAWS was not exposed to credit risk on its outstanding swap because the swap had a negative fair value. However, should interest rates change and the fair value of the swap become positive, SAWS would be exposed to credit risk in the amount of the swap's fair value. The swap counterparty, Bear Stearns, was rated AAA by Fitch's Ratings and Standard & Poor's and Aaa by Moody's Investor Service as of December 31, 2004. The swap agreement contains a collateral agreement with the counterparty. Collateralization of the fair value of the swap is required should Bear Stearns credit rating fall below the applicable thresholds in the agreement.

Basis Risk - SAWS is exposed to risk to the extent that the interest payments on its variable-rate bonds do not match the variable-rate payments received on the associated swap. SAWS mitigates this risk by (a) matching the notional amount and amortization schedule of the swap to the principal amount and amortization schedule of the Series 2003 Bonds, and (b) selecting an index for the variable-rate leg of the swap that is expected to match the interest rate resets on the Series 2003 Bonds over the life of the issue.

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(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)

E. San Antonio Water System (SAWS) (Continued)

Termination Risk - SAWS may terminate for any reason. Bear Stearns may terminate a swap if SAWS fails to perform under the terms of the agreement. The ongoing payment obligations under the swap are insured, and Bears Stearns cannot terminate as long as the insurer does not fail to perform. If at the time of the termination the swap has a negative fair value, SAWS would be liable to the counterparty for a payment equal to the swap's fair value.

Swap payments and associated debt - As of December 31, 2004, debt service requirements of the variable-rate debt and net swap payments, assuming current interest rates remain the same are below. As rates vary, variable-rate bond interest payments and net swap payments will vary.

Pay-Fixed, Receive-Variable Interest Rate Swap: Estimated Debt Service Requirements of Variable-Rate Debt Outstanding and Net Swap Payments				
Variable-Rate Bonds				
Year	Principal	Interest	Interest Rate Swap, net	Total
2005	\$ 2,080	\$ 2,335	\$ 2,609	\$ 7,024
2006	2,170	2,293	2,562	7,025
2007	2,275	2,249	2,513	7,037
2008	2,375	2,203	2,462	7,040
2009	2,485	2,155	2,408	7,048
2010-2014	14,235	9,975	11,146	35,356
2015-2019	17,780	8,401	9,387	35,568
2020-2024	22,220	6,435	7,190	35,845
2025-2029	27,770	3,977	4,443	36,190
2030-2033	27,125	1,004	1,122	29,251
Total	\$ 120,515	\$ 41,027	\$ 45,842	\$ 207,384

Stock Investment - The demutualization of Metropolitan Life Insurance on April 7, 2000 made SAWS, a policyholder, eligible to receive compensation for the membership interest for the dental plan provided as a benefit for employees. The demutualization compensation consisted of a distribution of 7,567 shares of MetLife, Inc. Common Stock. On the date of issue, the stock was priced at \$14.25 per share for a total value of \$108.

On October 26, 2001, with the demutualization of Principal Financial Group, Inc. SAWS received compensation for the membership interest for the life insurance provided as a benefit for employees and retirees. The demutualization compensation consisted of a distribution of 134,652 shares of Principal Financial Group, Inc. Common Stock. On the date of issuance, the stock was priced at \$23.35 per share for a total value of \$3,144. These two stock transactions have been recorded on the financial records of SAWS and in accordance with GASB Statement No. 31, an unrealized gain has been recorded in the amount of \$1,060 for Principal Financial Group, Inc. and \$52 for MetLife, Inc.

A summary of the SAWS Cash and Cash equivalents is provided at the conclusion of this note with a comparison to the Statement of Net Assets.

(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)

F. Summary of Cash and Cash Equivalents and Investments

A summary of cash and cash equivalents and investments are presented below as of year-end for the City, Fire and Police Pension, Retiree Health Care and its significant discretely presented Component Units, SAWS and CPS. The information is provided to give an indication of the proportionate amount of cash and investments held by each respective entity and to facilitate reconciliation to the statement of net assets.

Combined Cash, Cash Equivalents, and Investments				
	City ¹	SAWS ²	CPS ³	
Cash and Cash Equivalents	\$ 384,720	\$ 15,811	\$	171,213
Security Lending Collateral				
Cash and Cash Equivalents	177,712			
Investments	2,720,373	300,364		1,417,607
Less: Investments with original maturities of less than ninety days included in cash and cash equivalents	(242,931)	(8,407)		(163,369)
Total	\$ 3,039,874	\$ 307,768	\$	1,425,451
Totals from Statement of Net Assets and Statement of Fiduciary Net Assets				
Unrestricted:	City ¹	SAWS ²	CPS ³	
Cash and Cash Equivalents	\$ 362,098	\$ -	\$	50,920
Security Lending Collateral	177,712			
Investments	2,288,370	43,542		258,406
Total Unrestricted	2,828,180	43,542		309,326
Restricted:				
Cash and Cash Equivalents	22,622	15,811		120,293
Investments	189,072	248,415		995,832
Total Restricted	211,694	264,226		1,116,125
Total Cash and Cash Equivalents and Investments	\$ 3,039,874	\$ 307,768	\$	1,425,451

¹ The following amounts were held by the City in a fiduciary capacity and are excluded from the Statement of net assets: Cash and Cash Equivalents of \$117,895; Security Lending Collateral- and Cash Equivalents of \$177,712; Investments of \$1,742,213.

² For the fiscal year ended December 31, 2004.

³ For the fiscal year ended January 31, 2005.

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(amounts are expressed in thousands)

3. CASH AND CASH EQUIVALENTS AND INVESTMENTS (Continued)

F. Summary of Cash and Cash Equivalents and Investments (Continued)

The composition of Cash and Cash Equivalents included in the financial statements for the City and its major discretely presented Component Units as of each respective year-end is presented below.

	City	SAWS ¹	CPS ²
Deposits with Financial Institutions	\$ 30,220	\$ 7,213	\$ 6,979
Investments with Original Maturities of Less than Ninety Days	242,931	8,407	163,369
Cash with Pension/Retiree Healthcare Fiscal Agents	111,195		
Cash with Other Financial Agents	24		735
Petty Cash Funds	169	191	130
Cash On Hand	181		
Total Cash and Cash Equivalents	\$ 384,720	\$ 15,811	\$ 171,213

¹ For the fiscal year ended December 31, 2004.

² For the fiscal year ended January 31, 2005.

Cash with fiscal agents of the Fire and Police Pension Fund of the City of San Antonio have been approved by the Fund's Board of Directors and are invested as authorized by Texas State Statutes. Cash with fiscal agents of the Fire and Police Retiree Healthcare Fund of San Antonio have been approved by the Fund's Board of Directors and are invested as authorized by the Investment Policy Statement and Guidelines of the San Antonio Fire and Police Retiree Health Care Fund, San Antonio.

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(amounts are expressed in thousands)

4. CAPITAL ASSETS

Capital asset activity for governmental activities, to include Internal Service Funds, for the year ended September 30, 2005, is as follows:

Capital Assets - Governmental Activities					
Governmental Activities:	Beginning Balance	Increases	Decreases	Transfers	Ending Balance
Non-Depreciable Assets:					
Land	\$ 1,259,362	\$ 8,780	\$ -	\$ -	\$ 1,268,142
Construction in Progress	645,521	82,119	-	(112,877)	614,763
Total Non-Depreciable Assets	1,904,883	90,899	-	(112,877)	1,882,905
Depreciable Assets:					
Buildings	387,826	1,155		7,856	396,837
Improvements	77,732			29,301	107,033
Infrastructure	1,979,118			75,720	2,054,838
Machinery and Equipment	198,101	27,401	(9,441)		216,061
Total Depreciable Assets	2,642,777	28,556	(9,441)	112,877	2,774,769
Accumulated Depreciation:					
Buildings	(167,176)	(1,377)			(168,553)
Improvements	(37,353)	(4,101)			(41,454)
Infrastructure	(1,190,224)	(68,412)			(1,258,636)
Machinery and Equipment	(105,278)	(22,944)	7,750		(120,472)
Total Accumulated Depreciation	(1,500,031)	(96,834) ⁽¹⁾	7,750		(1,589,115)
Total Depreciable Assets, net	1,142,746	(68,278)	(1,691)	112,877	1,185,654
Total Capital Assets, net ⁽²⁾	\$ 3,047,629	\$ 22,621	\$ (1,691)	\$ -	\$ 3,068,559

¹ Depreciation expense was charged to governmental functions as follows:

General Government	\$ 6,323
Public Safety	5,654
Public Works	61,682
Health Services	365
Welfare	717
Culture and Recreation	5,477
Convention and Tourism	25
Urban Redevelopment and Housing	4,240
Depreciation on capital assets held by the City's internal service funds are charged to various functions based on asset usage	12,351
Total Depreciation Expense for Governmental Activities	\$ 96,834

² The capital assets of internal service funds are included in governmental activities. In fiscal year 2005, internal service funds capital assets increased by \$19,270, decreased by \$8,790, resulting in an ending balance of \$120,239. Depreciation expense of \$12,351 resulted in an ending accumulated depreciation balance of \$74,557, to arrive at net book value of \$45,682.

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(amounts are expressed in thousands)

4. CAPITAL ASSETS (Continued)

The City capitalizes interest incurred on construction projects, in accordance with Statement of Accounting Standard No. 62 issued by the Financial Accounting Standards Board. In fiscal year 2005, the City capitalized construction period interest for the Aviation and Parking funds in the amount of \$1,258 and \$95, respectively. Capital asset activity for business-type activities for the year ended September 30, 2005, is as follows:

Capital Assets - Business-Type Activities				
	Beginning Balance	Increases	Decreases	Ending Balance
Non-Depreciable Assets:				
Land:				
Aviation Fund	\$ 2,970	\$ -	\$ -	\$ 2,970
Parking Fund	8,125			8,125
Non-Major Fund	893			893
Total	11,988			11,988
Construction in Progress:				
Aviation Fund	107,750	19,224	(28,592)	98,382
Parking Fund	12,434	1,102	(10,207)	3,329
Non-Major Fund	436	162		598
Total	120,620	20,488	(38,799)	102,309
Total Non-Depreciable Assets	132,608	20,488	(38,799)	114,297
Depreciable Assets:				
Buildings:				
Aviation Fund	115,656	28,592		144,248
Parking Fund	18,985	10,207		29,192
Non-Major Fund	46			46
Total	134,687	38,799		173,486
Improvements:				
Aviation Fund	156,110			156,110
Parking Fund	1,283			1,283
Non-Major Fund	3,025			3,025
Total	160,418			160,418
Machinery and Equipment:				
Aviation Fund	10,299	587	(20)	10,866
Parking Fund	571	8		579
Non-Major Fund	3,743	296	(199)	3,840
Total	14,613	891	(219)	15,285
Total Depreciable Assets	309,718	39,690	(219)	349,189
Total Capital Assets	\$ 442,326	\$ 59,178	\$ (438)	\$ 491,066
Accumulated Depreciation:				
Buildings:				
Aviation Fund	(53,907)	(4,153)		(58,060)
Parking Fund	(8,412)	(736)		(9,148)
Non-Major Fund	(228)	(1)		(229)
Total	(62,547)	(4,890)		(67,437)
Improvements:				
Aviation Fund	(71,569)	(3,870)		(75,439)
Parking Fund	(478)	(41)		(519)
Non-Major Fund	(319)	(102)		(421)
Total	(72,366)	(4,013)		(76,379)
Machinery and Equipment:				
Aviation Fund	(7,718)	(851)	12	(8,557)
Parking Fund	(565)	(4)		(569)
Non-Major Fund	(2,736)	(267)	199	(2,804)
Total	(11,019)	(1,122)	211	(11,930)
Total Accumulated Depreciation	(145,932)	(10,025)	211	(155,746)
Total Depreciable Assets, net	\$ 163,786	\$ 29,665	\$ (8)	\$ 193,443
Total Capital Assets, net	\$ 278,540	\$ 59,170	\$ (446)	\$ 337,264

(amounts are expressed in thousands)

4. CAPITAL ASSETS (Continued)

CPS and SAWS capitalize interest incurred on construction projects, in accordance with Statement of Accounting Standard No. 62 issued by the Financial Accounting Standards Board. CPS and SAWS capitalized construction period interest in the amount of \$2,427 and \$15,918, respectively. Capital asset activity for CPS and SAWS is as follows:

Capital Assets - City Public Service ¹				
	Beginning Balance	Increases	Decreases	Ending Balance
City Public Service: Non-Depreciable Assets:				
Land	\$ 55,196	\$ 1,286	-	\$ 56,482
Land held for future use				
Nonutility property - land	12,599			12,599
Construction in Progress	248,585	222,134	(290,125)	180,594
Total Non-Depreciable Assets	316,380	223,420	(290,125)	249,675
Depreciable Capital Assets:				
Utility Plant in Service	6,709,503	324,623	(28,726)	7,005,400
Utility Property Leased	18,785			18,785
Nuclear Fuel	302,379	16,933	(126)	319,186
Total Depreciable Assets	7,030,667	341,556	(28,852)	7,343,371
Accumulated Depreciation:				
Utility Plant in Service	(2,458,254)	(236,686)	32,021	(2,662,919)
Utility Property Leased	(336)			(336)
Nuclear Fuel	(266,893)	(16,904)		(283,797)
Total Accumulated Depreciation	(2,725,483)	(253,590)	32,021	(2,947,052)
Total Depreciable Assets, net	4,305,184	87,966	3,169	4,396,319
Total Capital Assets, net	\$ 4,621,564	\$ 311,386	\$ (286,956)	\$ 4,645,994

Capital Assets - San Antonio Water System ²				
(Restated)	Beginning Balance	Increases	Decreases	Ending Balance
San Antonio Water System: Non-Depreciable Assets:				
Land	\$ 68,977	\$ 8,815	\$ (14,255)	\$ 63,537
Acquisition of Water Rights	18,077	725		18,802
Construction in Progress	428,226	224,216	(143,080)	509,362
Total Non-Depreciable Assets	515,280	233,756	(157,335)	591,701
Depreciable Assets:				
Utility Plant in Service	2,145,315	150,255	(2,068)	2,293,502
Machinery and Equipment	99,236	8,847	(5,031)	103,052
Total Depreciable Assets	2,244,551	159,102	(7,099)	2,396,554
Accumulated Depreciation:				
Utility Plant in Service	(683,594)	(53,092)	1,131	(735,555)
Machinery and Equipment	(60,098)	(7,554)	4,750	(62,902)
Total Accumulated Depreciation	(743,692)	(60,646)	5,881	(798,457)
Total Depreciable Assets, net	1,500,859	98,456	(1,218)	1,598,097
Total Capital Assets, net	\$ 2,016,139	\$ 332,212	\$ (158,553)	\$ 2,189,798

Beginning balances have been restated per SAWS December 31, 2004, CAFR

¹ For the fiscal year ended January 31, 2005² For the fiscal year ended December 31, 2004

(amounts are expressed in thousands)

4. CAPITAL ASSETS (Continued)

Construction-in-progress relating to the Capital Assets is comprised of the following:

Construction-In-Progress: Assets-Governmental Activities				
	Project Authorization	Expended to Sept. 30, 2005	Committed	Required Future Financing
Buildings	\$ 56,761	\$ 26,023	\$ 30,738	None
Streets and Bridges	378,060	297,530	80,530	None
Storm Drainage and Flood Prevention	157,681	117,120	40,561	None
Improvements Other Than Buildings	420,885	174,090	246,795	None
Total	\$ 1,013,387	\$ 614,763	\$ 398,624	

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(amounts are expressed in thousands)

5. RECEIVABLES AND PAYABLES

A. Disaggregation of Receivables and Payables

Receivables

Net receivables at September 30, 2005, were as follows:

	Accounts	Taxes	Notes and Loans	Accrued Interest	Other	Total Net Receivables
<u>Governmental Activities:</u>						
General Government	\$ 34,814	\$ 60,979	\$ -	\$ 3,430	\$ 680	\$ 99,903
Public Safety	23			88		111
Public Works	3,086			608		3,694
Health Services	9,321			4		9,325
Environmental Protection and Control	220			8		228
Culture and Recreation	544			355		899
Convention and Tourism	5,348			212		5,560
Urban Redevelopment and Housing	112			28		140
Welfare	17		5,347	23		5,387
Economic Development Opportunity	253			59		312
Total - Governmental Activities	\$ 53,738	\$ 60,979	\$ 5,347	\$ 4,815	\$ 680	\$ 125,559
<u>Business-Type Activities:</u>						
Airport System	\$ 2,366	\$ -	\$ -	\$ 75	\$ -	\$ 2,441
Parking Facilities	114			20		134
Non-Major Fund	4,177			19		4,196
Total - Business-Type Activities	\$ 6,657	\$ -	\$ -	\$ 114	\$ -	\$ 6,771

The receivable balances for General Government, Public Health Services, Environmental Protection and Control, and Convention and Tourism have been reduced by the estimated allowance for doubtful accounts of \$17,132, \$19,898, \$15, \$79, respectively, and General Government Taxes of \$3,632. The receivable balance for Business-Type Activities has been reduced by the estimated allowance for doubtful accounts of \$440.

The only receivables not expected to be collected within one year are \$4,727 of notes and loans receivable in Welfare.

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(amounts are expressed in thousands)

5. RECEIVABLES AND PAYABLES (Continued)

A. Disaggregation of Receivables and Payables (Continued)

Payables

Payables at September 30, 2005, were as follows:

	Accounts	Accrued Payroll	Total Payables
Governmental Activities:			
General Government	\$ 80,443	\$ 4,216	\$ 84,659
Public Safety	1,603	7,042	8,645
Public Works	14,437	690	15,127
Sanitation	1,282	764	2,046
Health Services	23	44	67
Culture and Recreation	3,033	941	3,974
Convention and Tourism	4,861	544	5,405
Urban Redevelopment and Housing	559	414	973
Welfare	9,097	870	9,967
Economic Development Opportunity	603	92	695
Total - Governmental Activities	\$ 115,941	\$ 15,617	\$ 131,558
Business-Type Activities:			
Airport System	\$ 7,320	\$ 487	\$ 7,807
Parking Facilities	532	109	641
Non-Major Fund	3,313	646	3,959
Total - Business-Type Activities	\$ 11,165	\$ 1,242	\$ 12,407

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(amounts are expressed in thousands)

5. RECEIVABLES AND PAYABLES (Continued)

B. Interfund Receivable and Payable Balances

The following is a summary of interfund receivables and payables for the City as of September 30, 2005:

Summary Table of Interfund Receivables and Payables As of September 30, 2005			
	Due From Other Funds	Due To Other Funds	
General Fund:			
Fiduciary Funds	\$	700	\$
Nonmajor Governmental Funds		43,987	
Nonmajor Enterprise Fund			1,664
Total General Fund		44,687	1,664
Debt Service Funds:			
Nonmajor Governmental Funds		1,539	
Total Debt Service Funds		1,539	
Airport System Fund:			
Airport Operating Fund from the Airport I&C Fund		539	
Airport Debt Service Fund from the Airport I&C Fund		4,938	
Airport I&C Fund to the Airport Operating Fund			539
Airport I&C Fund to Airport Construction Fund			4,938
Nonmajor Governmental Funds		2,228	
Total Airport System Fund		7,705	5,477
Parking Fund:			
Parking Debt Service from Parking Operating		4,171	
Parking Debt Service from Parking Debt Service		641	
Parking Debt Service from Parking Construction		33	
Parking Facilities from Parking Operating		2,724	
Parking Construction from Parking Debt Service		6,035	
Parking Operating to Parking Debt Service			4,171
Parking Debt Service to Parking Construction			6,035
Parking Debt Service to Parking Debt Service			641
Parking Construction to Parking Debt Service			33
Parking Operating to Parking Facilities			2,724
Nonmajor Governmental Funds			90
Total Parking Fund		13,604	13,694
Fiduciary Agency Funds:			
General Fund			700
Total Fiduciary Agency Funds			700
Internal Service Funds:			
Nonmajor Governmental Funds		353	
Internal Service Funds		13,277	13,277
Total Internal Service Funds		13,630	13,277
Nonmajor Governmental Funds:			
General Fund		1,664	
Airport Fund			43,987
Debt Service Fund			2,228
Internal Service Funds			1,539
Parking Fund		90	353
Nonmajor Governmental Funds			10
Total Nonmajor Governmental Funds		20,395	20,395
Nonmajor Enterprise Fund:		22,149	68,512
Nonmajor Governmental Funds			
Environmental Services Operating Fund from the I&C Fund		10	
Environmental Services I&C Fund to Operating Fund		409	409
Total Nonmajor Enterprise Fund		419	409
Total	\$	103,733	\$ 103,733

(amounts are expressed in thousands)

5. **RECEIVABLES AND PAYABLES (Continued)**

B. Interfund Receivable and Payable Balances (Continued)

As of September 30, 2005, the balances represent short-term loans resulting from (1) timing differences between the dates that transactions are recorded in the accounting system and (2) short-term borrowings at year-end. Of the \$44,687 due from other funds in the General Fund, \$43,598 is a result of overdraws of pooled cash. All amounts are expected to be paid within one year.

6. **LONG-TERM DEBT**

A. Primary Government (City)

1. **Governmental Activity Long-Term Debt**

The City's on-going capital improvement financing for infrastructure and "quality of life" purposes resulted in the issuance of additional indebtedness during fiscal year 2005. In April 2005, the City issued the following: \$116,170 in General Improvement Bonds and Refunding Bonds, Series 2005 and \$10,535 Combination Tax and Revenue Certificates of Obligations, Series 2005. The 2005 Obligations are payable from ad valorem taxes. The bonds are secured by a pledge of ad valorem taxes while the certificates are secured by a pledge of ad valorem taxes and revenues from certain revenues generating operations.

The net proceeds from the sale of the 2005 General Improvement Refunding Bonds, which included an original premium of \$9,031, were applied, together with a cash contribution from the City, to fund an escrow fund for the redemption, discharge, and defeasance of the refunded obligations. As a result of the 2005 refunding, the City will realize a total reduction of \$10,430 in debt service payments. Through the transaction, the City obtained a total economic gain (difference between the present values of the debt service payments on the old and new debt) of \$3,680.

The General Improvement Bond, Series 2005 will be utilized to refund a portion of the City's outstanding tax supported debt, fund capital improvements to include streets and pedestrian improvements; drainage improvements; park and recreation facilities improvements; library improvements; public health and safety improvements. The Series 2005 General Improvement Bonds are retired serially in the years 2010 through 2025 and bear interest rates ranging from 3.5% to 5.3%.

Proceeds of the Combination Tax and Revenue Certificates of Obligation, Series 2005 will be utilized to fund capital improvements to include public safety, including constructing, renovating and improving existing fire stations; street, sidewalk, bridge, and drainage improvements; improvements and renovations to existing municipal facilities; acquiring, constructing, and renovating park facilities; constructing improvements for flood control, dams, landscaping, amenities along the San Antonio River; the purchase of materials, supplies, machinery, land, and rights-of-way for authorized needs and purposes relating to public safety, drainage, street, parks, and public works purposes; and professional services related to the construction and financing of the aforementioned projects. The certificates are retired serially in the years 2005 through 2025 and bear interest rates ranging from 4.0% to 5.3%.

In May 2005, the City issued \$2,900 Taxable Combination Tax and Revenue Certificates of Obligation, Series 2005A. The certificates will be utilized to fund Alamodome improvement projects. The series 2005A certificates are retired serially in the year 2007 and bear the interest rate 4.6%.

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(amounts are expressed in thousands)

6. **LONG-TERM DEBT (Continued)**

A. Primary Government (City) (Continued)

1. **Governmental Activity Long-Term Debt (Continued)**

Additionally in April 2005, the City issued \$61,060 of Municipal Drainage Utility System Revenue Bonds, Series 2005. Delivery of the bonds occurred on April 15, 2005. Pursuant to authority conferred by the Municipal Drainage Utility System Act, the City Council adopted an ordinance in 1997 declaring the drainage of the City to be a public utility, enabling the City to bill, along with other municipal utility system billings, a separate charge against lots and tracts of benefited property in the City for drainage services. Revenues are pledged to the payment of the Bonds to the extent and in the manner specified in the ordinance. The obligations bear interest ranging from 2.600% to 4.620% and will be retired in the years 2006 through 2030.

Proceeds of the 2005 Municipal Drainage Utility System Revenue Bonds will be used to finance the costs of drainage improvements, including the acquisition, construction, and repair of structures, equipment, and facilities for the City's Municipal Drainage Utility System.

The City of San Antonio issued the following: \$129,930 Contract Revenue Empowerment Zone Bonds, Series 2005B for Texas Convention Center Hotel Finance Corporation. Hotel Investments, L.P. will be loaned the proceeds from the Series 2005 bonds by the Texas Convention Center Hotel Finance Corporation. Hotel Investments, L.P. will use the proceeds of the Series 2005 Bonds to finance a portion of the costs to design, develop, construct, equip, furnish, and open a full-service hotel. The bonds are secured by pledged Hotel Occupancy Tax revenues and are payable solely from payments made by the City sufficient to pay principal and interest on the bonds. As of September 30, 2005, the Texas Convention Center Hotel Finance Corporation Empowerment Zone Bonds and Contract Revenue Bonds outstanding balances are \$129,930 and \$78,215.

The Starbright Industrial Development Corporation was created to act on behalf of the City in the promotion and development of commercial, industrial and manufacturing enterprises to promote and encourage employment and public welfare, including but not limited to the acquisition of land. The City of San Antonio, Starbright Industrial Development Corporation Contract Revenue Bonds, Series 2003 were issued to finance the acquisition and conveyance of land to Toyota Motor Manufacturing North America, Inc. for the construction of a training facility. The bonds are pledged by dedicated revenues transferred to the City by the City Public Service (CPS) Board and are payable solely from payments made by the City sufficient to pay principal and interest on the bonds. As of September 30, 2005, the Starbright Industrial Development Corporation contract Revenue Bonds outstanding totaled \$24,685.

Prior Years Defeased Debt

In preceding years, the City refunded, prior to maturity, certain General Obligation Bonds, Revenue Bonds, and Certificates of Obligation. The refunding bonds were utilized to purchase securities, which are direct obligations of United States of America (the Purchase Securities). The Purchased Securities plus cash were deposited into irrevocable escrow funds in amounts scheduled to mature in principal amounts that, when added to interest earned on the Purchased Securities plus remaining balances in the escrow fund, are fully sufficient to make timely payment on the principal, premium if any, and interest scheduled to come due on the refunded obligations. The refunded obligations represent a legal defeasance and are no longer a liability of the City, therefore, they are not included in the City's financial statements. On September 30, 2005, \$261,173 of previously defeased bonds were outstanding.

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(amounts are expressed in thousands)

6. LONG-TERM DEBT (Continued)

A. Primary Government (City) (Continued)

1. Governmental Activity Long-Term Debt (Continued)

The following table is a summary of changes for the year ended September 30, 2005, for Governmental Activity Debt:

Governmental Activity Long-Term Debt (At Valued Tax Pledge)									
Issue	Original Amount	Fiscal Year	Interest Rate (%)	Balance Outstanding October 1, 2004	Additions During Year	Debtors During Year	Balance Outstanding September 30, 2005		
General Obligation Bonds ¹									
1996 Refunding	\$ 112,978	2006	7.250-7.400	\$ 3,681	\$	\$ 1,046	\$	1,735	
1996 Refunding	53,330	2005	5.100	1,585		1,585		46,240	
1996 Refunding	82,235	2006	4.800-6.000	40,750		3,310		2,150	
1998 Refunding	6,000	2008	6.700	2,790		640		17,790	
1998 Refunding	30,885	2008	4.500-5.000	26,715		9,325		17,795	
1998 Refunding	52,000	2008	5.300-6.000	20,735		2,960		30,280	
1998 Refunding	42,955	2009	4.000-5.250	40,625		10,345		3,140	
1999	12,000	2011	5.000	10,860		7,720		18,375	
2000	27,565	2020	4.500-5.000	14,715		6,140		7,635	
2000A	15,615	2021	5.250-5.375	14,715		3,045		48,210	
2001	84,945	2002	3.000-5.250	34,380		35,160		21,815	
2001 Forward Refunding	239,910	2013	5.000-5.250	200,525		21,400		32,045	
2002	55,880	2003	3.000-5.500	51,565		2,025		55,665	
2003	40,095	2004	2.750-5.000	34,290		2,275		33,570	
2004	55,710	2016	3.500-5.000	55,665				116,170	
2004A	33,570	2024	2.375-4.750	33,570				658,450	
2005	116,170	2025	3.500-5.250	\$ 655,141	\$ 116,170	\$ 112,861	\$		
Subtotal	\$ 1,071,573			\$ 440	\$	\$ 440	\$	0	
Tax-Exempt Certificates of Obligation									
Series 1996	\$ 8,415	2005	5.200	1,125		550		575	
Series 1996A	12,515	2006	4.650-4.750	2,715		960		1,755	
Series 1998	4,315	2018	4.700-5.000	28,555		12,615		15,940	
Series 1998A	36,535	2019	4.000-5.250	3,830		2,720		1,110	
Series 1999	4,230	2011	5.750	7,610		1,890		5,720	
Series 2000	8,490	2020	4.500-5.000	8,285		3,980		4,305	
Series 2000A	8,810	2021	5.250-5.375	6,310		245		6,065	
Series 2000C	6,415	2020	4.000-5.250	58,490		4,810		53,680	
Series 2001	65,195	2014	5.000-5.500	67,585		1,680		65,905	
Series 2002	69,990	2023	3.000-5.500	29,525		440		10,535	
Series 2002A	29,525	2024	2.000-5.000	29,525				194,675	
Series 2005	10,535	2025	4.000-5.250	\$ 214,470	\$ 10,535	\$ 30,330	\$	1,300	
Subtotal	\$ 304,910			\$ 1,575	\$	\$ 275	\$	1,040	
Revenue Bonds ²								1,610	
Series 1996	\$ 6,160	2009	6.500-6.000	1,545		305		2,900	
Series 1996A	7,275	2008	6.000	1,660		50		6,850	
Series 2000B	1,255	2021	7.490-7.550	461				86,897	
Series 2005A	2,900	2007						45,090	
Subtotal	\$ 18,190			\$ 4,580	\$ 2,900	\$ 630	\$	12,300	
Revenue Bonds ²								10,390	
Series 1996 Occupancy Tax	\$ 182,012	2026	5.100-6.020	\$ 86,897	\$	1,065		110,625	
2003 Drought	44,150	2028	3.500-5.000	43,115				78,215	
2005 Drought	61,000	2030	3.900-5.250	61,000				24,685	
Series 2001 Municipal Facility Corp.	14,465	2020	3.900-5.250	12,870		570		586,153	
Series 2004A	10,390	2029	5.000	10,390				1,416,177	
Series 2004B	111,425	2020	2.000-5.000	111,425		800			
Convention Center 2005A	129,930	2039	5.000	129,930					
Convention Center 2005B	78,215	2028	4.500-5.310	78,215					
Starlight Industrial Dev Corp	24,685	2033	2.180-5.110	24,685					
Subtotal	\$ 656,332			\$ 264,497	\$ 24,685	\$ 2,435	\$		
Total	\$ 2,011,005			\$ 1,138,888	\$ 423,495	\$ 146,256	\$		

¹ Accretion of interest on 1998 General Improvement Refunding Bonds for Fiscal Year 2005 has resulted in an increase of \$8,709 in General Obligation Bonds Payable.

This increase is reflected on the Statement of Net Assets but is not shown on above table.

² A portion of the Hotel Occupancy Tax Revenue Bonds, Series 1996 was sold as Capital Appreciation Bonds (CABS). Interest on the CABS will accrete from date of delivery and will be payable only at maturity or redemption. Interest accreted through Fiscal Year 2005 has resulted in an increase of \$13,536 in Revenue Bonds Payable. This increase is reflected on the Statement of Net Assets but is not shown on above table.

6. LONG-TERM DEBT (Continued)

A. Primary Government (City) (Continued)

1. Governmental Activity Long-Term Debt (Continued)

Annual Requirements

The annual requirements to amortize all General Obligation Bonds, Tax Exempt Commercial Paper, Certificates of Obligation, and Hotel Occupancy Tax Revenue Bonds outstanding as of September 30, 2005, are as follows:

Principal and Interest Requirements									
Year Ending September 30,	General Obligation Bonds		Certificates of Obligation		Revenue Bonds		Hotel Occupancy Tax		Total Annual Requirements
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	
	\$	\$	\$	\$	\$	\$	\$	\$	
2006	44,850	37,146	11,900	9,600	4,385	26,975			134,856
2007	49,875	30,551	17,085	8,886	5,930	26,825			139,152
2008	53,370	28,037	16,370	8,112	6,665	26,621			139,175
2009	55,015	23,261	16,445	7,333	9,505	24,200			135,759
2010	59,055	20,958	15,340	6,609	12,630	23,878			138,470
2011-2015	214,995	68,478	70,910	21,018	53,043	113,756			542,200
2016-2020	123,725	29,878	32,610	9,482	81,744	102,064			379,503
2021-2025	57,565	4,789	20,865	1,928	118,880	77,650			281,677
2026-2030					116,050	47,720			163,770
2031-2035					92,180	24,802			116,982
2036-2039					55,140	7,056			62,196
Total	\$ 658,450	\$ 243,098 ¹	\$ 201,525	\$ 72,968	\$ 556,152 ²	\$ 501,547			\$ 2,233,740
Total Principal & Interest Payable Within One Year									
Principal	\$ 44,850	\$ 11,900	\$ 4,385						\$ 61,135
Interest	37,146	9,600	26,975						73,721
Total	\$ 81,996	\$ 21,500	\$ 31,360						\$ 134,856

¹ Accretion of interest on the 1998 General Improvement Bonds through the year ended September 30, 2005, has resulted in an increase of \$8,709 in General Obligation Bonds Payable. Total interest to be accreted is reflected in the interest portion of the above table.

² A portion of the Hotel Occupancy Tax Revenue Bonds (Series 1996) was sold as Capital Appreciation Bonds (CABS). Interest on the CABS accretes from the date of delivery and will be payable only at maturity or redemption. The interest accreted through September 30, 2005, has resulted in an increase of \$13,536 in Revenue Bonds Payable. Total interest to be accreted is reflected in the interest portion of the above table.

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(amounts are expressed in thousands)

(amounts are expressed in thousands)

6. LONG-TERM DEBT (Continued)

A. Primary Government (City) (Continued)

1. Governmental Activity Long-Term Debt (Continued)

Authorized But Unissued General Obligation Debt				
Authorization Date	Purpose	Amount Authorized	Bonds Previously Issued	Bonds Authorized But Unissued
1-26-80 1	Drainage and Flood Control	\$ 21,637	\$ 17,413	\$ 4,224
1-26-80 1	Fire Protection	4,257	2,125	2,132
1-26-80 1	Libraries	4,978	3,926	1,052
1-26-80 1	Street, Bridge, and Related Improvements	43,287	34,035	9,252
5-07-94	Street Improvements	25,600	25,600	
5-07-94	Drainage Improvements	34,400	34,400	
5-07-94	Parks and Recreation	41,600	41,600	
5-01-99	Streets and Pedestrian Improvements	41,300	41,300	
5-01-99	Drainage	19,000	19,000	
5-01-99	Flood Control	12,200	12,200	
5-01-99	Parks and Recreation	24,200	24,200	
5-01-99	Library System	13,200	13,200	
5-01-99	Public Safety	30,300	30,300	
11-04-03 2	Street & Pedestrian	29,398	18,828	10,570
11-04-03 2	Drainage	18,913	15,492	3,421
11-04-03 2	Parks and Recreation	27,224	24,522	2,702
11-04-03 2	Library System	3,965	3,065	900
11-04-03 2	Public Health & Safety	35,500	4,768	30,732
Total		\$ 430,959	\$ 365,974	\$ 64,985

¹ In addition to the debt authorized on May 1, 1999, and November 2003, the City has authority pursuant to an election held on January 26, 1980, to issue \$16,660 in bonds. The City does not currently intend to issue the bonds authorized in 1980.

² An additional \$115,000 was authorized November 4, 2003, of which \$48,325 remains to be issued.

Debt Limitation

The amount of debt that the City may incur is limited by City Charter and by the Constitution of the State of Texas. The City Charter establishes a limitation on the general obligation debt supported by ad valorem taxes to an amount not to exceed 10.0% of the total assessed valuation. The total assessed valuation for the fiscal year 2005 was \$51,824,208, which provides a debt ceiling of \$5,182,420. The total outstanding debt that is secured by an ad valorem tax pledge is \$872,090.

The Constitution of the State of Texas provides that the ad valorem taxes levied by the City for debt service and maintenance and operation purposes shall not exceed \$2.50 for each one hundred dollars of assessed valuation of taxable property. There is no limitation within the \$2.50 rate for interest and sinking fund purposes; however, it is the policy of the Attorney General of the State of Texas to prohibit the issuance of debt by a city if such issuance produces debt service requirements that exceed the amount that can be paid from \$1.50 tax rate calculated at 90.0% collections.

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(amounts are expressed in thousands)

6. LONG-TERM DEBT (Continued)

A. Primary Government (City) (Continued)

1. Governmental Activity Long-Term Debt (Continued)

Leases

The City leases property and equipment from others. Leased property having elements of ownership are recorded in the government-wide financial statements. The related obligations, in amounts equal to the present value of minimum lease payments payable during the remaining term of the leases, are also recorded in the government-wide financial statements. Other leased property, not having elements of ownership, are classified as operating leases. Both capital and operating lease payments are recorded as expenditures when matured in the governmental fund financial statements. Total expenditures for operating leases for the fiscal year ended September 30, 2005, were approximately \$2,886.

The City has entered into various lease purchase agreements for the acquisition of computers, copiers, fire trucks, golf equipment, public works equipment, a high-capacity trailer, and a hazardous materials vehicle. These lease agreements qualify as capital leases for accounting purposes and have been recorded at the present value of their future minimum lease payments as of the date of inception. Payments on each of the lease purchases will be made from budgeted annual appropriations to be approved by the City Council.

The assets acquired through capital leases for governmental activities are as follows:

Asset:	
Machinery and Equipment	\$21,157
Less: Accumulated Depreciation	(6,718)
Total	<u>\$14,439</u>

As of September 30, 2005, the City (excluding discretely presented component units) had future minimum lease payments under capital and operating leases with a remaining term in excess of one year for governmental activities as follows:

Leases - Governmental Activities			
Governmental Activities: Fiscal year ending September 30:		Capital Leases	Operating Leases
2006	\$	2,602	\$ 2,581
2007		2,153	1,457
2008		1,571	967
2009		771	943
2010		560	728
2011-2015			3,512
2016-2020			3,222
2021-2025			1,126
Future Minimum Lease Payments		<u>7,657</u>	<u>\$ 14,536</u>
Less: Interest		(425)	
Present Value of Future Minimum Lease Payments		<u>7,232</u>	
Less: Current Portion		(2,406)	
Capital Leases, net of current portion		<u>\$ 4,826</u>	

(amounts are expressed in thousands)

6. LONG-TERM DEBT (Continued)

A. Primary Government (City) (Continued)

2. Business-Type Long-Term Debt

Business-Type long-term debt applies to those City operations that relate to business and quasi-business activities where net income and capital maintenance are measured (Enterprise and Internal Service Funds). Long-term debt, which is to be repaid from proprietary funds resources, is reported in the respective proprietary fund. The long-term indebtedness of the City's Enterprise Funds is presented in the discussion that follows.

Airport System – The Airport System includes the City of San Antonio International Airport and Stinson Municipal Airport and all land, buildings, structures, equipment, and facilities pertaining thereto. The Airport System's long-term debt is equally and ratably secured solely by a first lien on and pledge of the Gross Revenues of the Airport System. Gross Revenues of the Airport System include all revenues of any nature derived from contracts or use agreements with airlines and other users of the System and its facilities.

On April 15, 2005, the City issued \$38,085 of System Revenue Improvement Bonds, Series 2005. Delivery of the bond occurred on May 24, 2005. The proceeds of the bonds will be utilized to acquire and construct improvements to the San Antonio International Airport. The bonds are special obligations of the City payable from gross revenues of the City's Airport System. Proceeds will be combined with a cash contribution from the City and used to refund other Airport System obligations. The bonds are retired serially in years 2006 to 2030 and bear interest rates ranging from 3.375% to 5.250%.

Parking System – The Parking System operation includes the ownership and operation of parking facilities, parking lots, parking meters, and retail/office space. Long-term debt is allocated to the Parking System on a pro-rata basis from proceeds received from the issuance of general obligation and certificate of obligation debt and is paid from revenues derived from the operation of the Parking System. This allocated debt is additionally secured by an ad valorem tax pledge. The bonds are payable from and secured by a first lien on and a pledge of the gross revenues derived from the ownership and operation of the City's Parking System.

Capitalized Interest Costs

Interest costs incurred on revenue bonds, general obligation bonds, and other borrowings totaled \$14,616. For fiscal year 2005, the amounts of \$1,258 and \$95 were capitalized for the Airport and Parking systems, respectively, as part of the cost of additions to the Airport and Parking systems.

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(amounts are expressed in thousands)

6. LONG-TERM DEBT (Continued)

A. Primary Government (City) (Continued)

2. Business-Type Long-Term Debt (Continued)

The following table is a summary of changes in revenue bonds, general obligation bonds, and tax-exempt certificates of obligation for the fiscal year ended September 30, 2005.

Issues	Business-Type Long-Term Debt						
	Balance			Deletions			Balance
	Original Amount	Final Principal Payment	Interest Rates (%)	Outstanding October 1, 2004	Additions During Year	During Year	September 30, 2005
Airport System							
Revenue Bonds:							
Series 1996	\$ 38,000	2014	5.700-5.750	\$ 18,325	\$ -	\$ 350	\$ 17,975
Series 2001	17,795	2016	5.375	17,795	-	-	17,795
Series 2002	92,470	2027	5.000-5.750	92,470	-	1,095	91,375
Series 2002 PFC	37,575	2027	4.000-5.750	35,995	-	845	35,150
Series 2003 Refunding	50,230	2013	5.500-6.000	46,360	-	4,080	42,280
Series 2003-A	8,175	2006	2.000-2.250	4,210	-	2,020	2,190
Series 2003-B	3,255	2009	2.300-3.000	3,255	-	-	3,255
Series 2005	38,085	2030	3.375-5.250	-	38,085	-	38,085
Subtotal	\$ 285,585			\$ 218,410	\$ 38,085	\$ 8,390	\$ 248,105
Parking System							
Revenue Bonds:							
Series 2000	\$ 24,845	2024	5.000-5.750	\$ 24,445	\$ -	\$ 450	\$ 23,995
General Obligation Bonds:							
Series 2004A Refunding	13,245	2016	1.400-4.650	13,245	-	1,130	12,115
Subtotal	\$ 38,090			\$ 37,690	\$ -	\$ 1,580	\$ 36,110
Total	<u>\$ 323,675</u>			<u>\$ 256,100</u>	<u>\$ 38,085</u>	<u>\$ 9,970</u>	<u>\$ 284,215</u>

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(amounts are expressed in thousands)

6. LONG-TERM DEBT (Continued)

A. Primary Government (City) (Continued)

2. Business-Type Long-Term Debt (Continued)

The annual requirements to amortize long-term debt for the City's Enterprise Funds related to revenue bonds, general obligations, and certificates of obligation outstanding at September 30, 2005, are as follows:

Business-Type Long-Term Debt							
Year End Sept. 30:	Airport System			Parking System			
	Principal	Interest	Total	Principal	Interest	Total	
2006	\$ 9,615	\$ 13,246	\$ 22,861	\$ 1,930	\$ 1,747	\$ 3,677	
2007	9,605	12,819	22,424	1,720	1,692	3,412	
2008	10,155	12,342	22,497	1,790	1,632	3,422	
2009	11,595	11,831	23,426	1,950	1,565	3,515	
2010	12,210	11,237	23,447	1,050	1,492	2,542	
2011-2015	68,930	44,773	113,703	11,140	7,746	18,886	
2016-2020	45,480	27,520	73,000	8,675	3,625	12,300	
2021-2025	49,445	15,848	65,293	7,855	1,162	9,017	
2026-2030	31,070	3,215	34,285				
Total	\$ 248,105	\$ 152,831	\$ 400,936	\$ 36,110	\$ 20,661	\$ 56,771	

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(amounts are expressed in thousands)

6. LONG-TERM DEBT (Continued)

A. Primary Government (City) (Continued)

2. Business-Type Long-Term Debt (Continued)

Leases

The City has entered into various lease purchase agreements for the acquisition of computers, copiers, fire trucks, golf equipment, public works equipment, a high-capacity trailer, and a hazardous materials vehicle. These lease agreements qualify as capital leases for accounting purposes and have been recorded at the present value of their future minimum lease payments as of the date of inception. Payments on each of the lease purchases will be made from budgeted annual appropriations to be approved by the City Council.

The assets acquired through capital leases for business-type activities are as follows:

Asset:	
Machinery and Equipment	\$ 709
Less: Accumulated Depreciation	(375)
Total	<u>\$ 334</u>

As of September 30, 2005, the City (excluding discretely presented component units) had future minimum payments under capital leases with a remaining term in excess of one year for business-type activities as follows:

Leases - Business-Type Activities: Nonmajor Enterprise Fund	
Proprietary Activities	
Fiscal year ending September 30:	
2006	\$ 156
2007	117
Future Minimum Lease Payments	273
Less: Interest	(10)
Present Value of Future Minimum Lease Payments	263
Less: Current Portion	(148)
Capital Leases, net of current portion	<u>\$ 115</u>

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(amounts are expressed in thousands)

6. LONG-TERM DEBT (Continued)

A. Primary Government (City) (Continued)

3. Governmental and Business-Type Long-Term Debt

Long-Term Obligations and Amounts Due Within One Year

Governmental Activities:	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Bonds Payable:					
General Obligation Bonds	\$ 655,141	\$ 116,170	\$ 112,861	\$ 658,450	\$ 44,850
Tax-Exempt Certificates of Obligation	214,470	10,535	30,330	194,675	11,900
Taxable Certificates of Obligation	4,580	2,900	630	6,850	
Revenue Bonds	264,697	293,890	2,435	556,152	4,385
Unamortized (Discount)/Premium	1,138,888	423,495	146,256	1,416,127	61,135
Deferred Amount on Refunding	40,343	12,904	3,448	49,799	3,766
	(15,863)	(5,058)	(7,082)	(13,839)	(6,538)
Total Bonds Payable	1,163,368	431,341	142,622	1,452,087	58,363
Other Liabilities:					
Accrued Arbitrage Rebate Payable	968	720		1,688	695
Capital Leases	7,126	3,236	3,130	7,232	2,406
Compensated Absences	121,536	57,059	49,942	128,653	46,029
Notes Payable		1,664	295	1,369	1,369
Total Other Liabilities	129,630	62,679	53,367	138,942	50,499
Total Governmental Activities	\$ 1,292,998	\$ 494,020	\$ 195,989	\$ 1,591,029	\$ 108,862
Business-Type Activities:					
Bond Payable:					
General Obligation Bonds	\$ 13,245	\$ 0	\$ 1,130	\$ 12,115	\$ 1,330
Revenue Bonds	242,855	38,085	8,840	272,100	10,215
	256,100	38,085	9,970	284,215	11,545
Unamortized (Discount)/Premium	1,984	1,310	282	3,012	
Deferred Amount on Refunding	(5,685)		(632)	(5,053)	
Total Bonds Payable	252,399	39,395	9,620	282,174	11,545
Other Payables:					
Aviation	3,084	1,453	2,972	1,565	1,565
Parking	519		512	7	7
Nonmajor Fund	1,051		21	1,030	200
Total Other Payables	4,654	1,453	3,505	2,602	1,772
Capital Leases-Nonmajor Fund	406		143	263	148
Compensated Absences	1,974	1,697	1,669	2,002	334
Total Other Liabilities	7,034	3,150	5,317	4,867	2,254
Total Business-Type Activities	\$ 259,433	\$ 42,545	\$ 14,937	\$ 287,041	\$ 13,799

The accreted interest through Fiscal Year 2005 has resulted in an increase of \$13,536 in Hotel Tax Revenue Bonds Payable in governmental activities and an increase of \$8,709 in General Obligation Bonds Payable. The accreted interest in the amount of \$22,245 is reflected on the Statement of Net Assets, but is not reflected in this table.

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(amounts are expressed in thousands)

6. LONG-TERM DEBT (Continued)

A. Primary Government (City) (Continued)

3. Governmental and Business-Type Long-Term Debt (Continued)

Compensated Absences

The following is a summary of compensated absences for the year ended September 30, 2005:

Fund Type	Governmental Activities				
	Short-Term Available	Short-Term Remaining	Total	Short-Term	Total
Governmental Funds	\$ 6,292	\$ 39,532	\$ 45,824	\$ 81,600	\$ 127,424
Internal Service Funds		205	205	1,024	1,229
Total Governmental Activities	\$ 6,292	\$ 39,737	\$ 46,029	\$ 82,624	\$ 128,653

The General Fund, which houses approximately 65.0% of the City's employees, has typically been used in prior years to liquidate the liability for compensated absences. However, the fund which liquidates compensated absences, is the same fund that the employee's salary is charged to throughout the year.

Business-Type Activities				
Fund	Short-Term	Long-Term	Total	
Airport	\$ 174	\$ 868	\$ 1,042	
Parking	16	82	98	
Non-Major Fund	144	718	862	
Total Business-Type Activities	\$ 334	\$ 1,668	\$ 2,002	

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(amounts are expressed in thousands)

6. LONG-TERM DEBT (Continued)

A. Primary Government (City) (Continued)

3. Governmental and Business-Type Long-Term Debt (Continued)

Conduit Debt Obligations

The City facilitates the issuance of bonds to enable the San Antonio Industrial Development Authority, Health Facilities Development Corporation, and the Education Facilities Corporation (formerly known as Higher Education Authority), component units of the City, to provide financial assistance to various entities for the acquisition, construction, or renovation of facilities deemed to be in the public interest. The bonds are secured by the property financed and are payable solely from payments received on the underlying mortgage loans. Upon repayment of the bonds, ownership of the acquired property transfers to the entity served by the bond issuance. As of September 30, 2005, there were 36 series of Industrial Revenue Bonds, 16 series of Health Facilities Development Bonds, and 13 series of Education Facility Revenue Bonds outstanding. The aggregate principal amount payable for the one series of Industrial Revenue Bonds, the one series of Health Facilities Development Bonds, and the four series Education Facility Revenue Bonds issued after October 1, 1997 was \$5,500, \$7,700, and \$60,940, respectively.

The City also facilitates the issuance of tax-exempt revenue bonds to enable the San Antonio Housing Finance Corporation to provide financing of residential developments for persons of low and moderate income. The bonds are secured by the property financed and are payable solely from and secured by a pledge of rental receipts. As of June 30, 2005, 27 series of tax-exempt revenue bonds were outstanding, with an aggregate principal amount payable of \$204,772 and an aggregate principal amount issued of \$224,775.

To provide for the acquisition and construction of certain airport facilities, the City has issued Special Facilities Airport Revenue Bonds, Series 1995 and Special Airport Facilities Revenue Refunding Bonds, Series 1999. The bonds are payable pursuant to lease agreements, which stipulate that various commercial entities are obligated to pay amounts to a third-party trustee in-lieu of lease payments to the City. These payments are sufficient to pay when due the principal, premium, interest on, and purchase price of the bonds. The aggregate principal amount payable for the Special Facilities Airport Revenue Bonds, Series 1995 and for the Special Airport Facilities Revenue Refunding Bonds, Series 1999 at September 30, 2005, was \$0 and \$4,000, respectively.

Neither the City, the State of Texas, nor any political subdivision of the State of Texas, is obligated in any manner for repayment of the aforementioned bonds or loans. Accordingly, the bonds and loans are not reported as liabilities in the accompanying financial statements.

The City entered into an agreement with the Greater Kelly Development Authority (GKDA) to fund renovations at Kelly Air Force Base, in the amount of \$20,000. The funding for the loan is provided by the Department of Housing and Development (HUD) through a section 108 Loan. The loan is secured by pledged GKDA revenues and property and are payable solely from payments received by the GKDA. As of September 30, 2005, the aggregate amount of the outstanding loan totaled \$17,660.

B. City Public Service (CPS)

As of January 31, 2005, the Bond Ordinances for New Series Bonds issued on and after August 6, 1992, contain, among others, the following provisions:

Funds in CPS' General Account shall be pledged and appropriated to be used in the following priority: (a) for maintenance and operating expenses of the systems, (b) for payments of the New Series Bonds, (c) for the payment of any obligations inferior in lien to the New Series Bonds which may be issued, (d) for an amount equal to 6.0% of the gross revenues of the systems to be deposited in the Repair and Replacement Account, (e) for cash payments and benefits to the City not to exceed 14.0% of the gross revenues of the systems, and (f) any remaining net revenues in the General Account to the Repair and Replacement Account.

(amounts are expressed in thousands)

6. LONG-TERM DEBT (Continued)

B. City Public Service (CPS) (Continued)

The maximum amount in cash to be transferred or credited to the General Fund of the City from the net revenues of the systems during any fiscal year shall not exceed 14.0% of the gross revenues of the systems less the value of gas and electric services of the systems used by the City for municipal purposes and the amounts expended during the fiscal year for additions to the street lighting system. The percentage of gross revenues of the systems to be paid over or credited to the General Fund of the City each fiscal year shall be determined (within the 14.0% limitation) by the governing body of the City.

The net revenues of the systems are pledged to the payment of principal and interest on the New Series Bonds. All New Series Bonds and the interest thereon shall have a first lien upon the net revenues of the systems.

The City agrees that it will at all times maintain rates and charges for the sales of electric energy, gas, or other services furnished, provided, and supplied by the systems to the City and all other consumers that shall be reasonable and nondiscriminatory and that will produce income and revenues sufficient to pay:

- (a) all maintenance and operating expenses, depreciation, replacement and betterment expenses, and other costs as may be required by Chapter 1502, as amended, Texas Government Code;
- (b) the interest on and principal of all New Series Bonds, as and when the same shall become due, and for the establishment and maintenance of the funds and accounts created for the payment and security of the New Series Bonds;
- (c) the interest on and principal of the Prior Lien Bonds, including the Junior Lien Obligations and any Additional Junior Lien Obligations hereafter issued (all as defined in the New Series Bond Ordinances), as and when the same shall become due, and for the establishment and maintenance of the funds and accounts created for the payment and security of the Junior Lien Obligations and any Additional Junior Lien Obligations;
- (d) to the extent the same are reasonably anticipated to be paid with available revenues (as defined in the ordinance authorizing the Commercial Paper), the interest on and principal of all Notes (as defined in said ordinance), and the credit agreement (as defined in said ordinance); and
- (e) a legal debt or obligation of the systems as and when the same shall become due.

Revenue Bonds

A summary of revenue bonds is as follows:

City Public Service Revenue Bonds		
Bond Series	Weighted-Average Interest Rate on Outstanding Bonds	2005
Tax Exempt New Series Bonds, 1992-2003; 2006-2021	5.0%	\$ 2,116,345
Taxable New Series		
Taxable New Series Bonds, 1998 & 2000; 2006-2021	6.7%	134,880
	5.1%	2,251,225
Tax-exempt Variable Rate Series Bonds, 2003, 2029-2033		410,000
Total Revenue Bonds outstanding		2,661,225
Less: Current maturities of bonds		127,255
Total Revenue Bonds, net of current maturities		\$ 2,533,970

(amounts are expressed in thousands)

6. LONG-TERM DEBT (Continued)

B. City Public Service (CPS) (Continued)

Principal and interest amounts due for the next five years and thereafter to maturity are:

City Public Service				
Principal and Interest Requirements				
Year	Principal	Interest	Total	
2006	\$ 127,255	\$ 127,008	\$ 254,263	
2007	135,155	120,387	255,542	
2008	142,155	113,407	255,562	
2009	148,570	106,167	254,737	
2010	154,790	98,485	253,275	
2011-2015	824,195	360,383	1,184,578	
2016-2020	657,315	165,914	823,229	
2021-2025	101,790	44,013	145,803	
2026-2030	220,000	27,693	247,693	
2031-2033	150,000	5,640	155,640	
Totals	\$ 2,661,225	\$ 1,169,097	\$ 3,830,322	

In May 2003, CPS issued \$250,000 of variable rate Junior Lien Revenue Bonds. The bonds were issued initially in a weekly interest mode at par value. Of the proceeds, \$111,900 was issued to reimburse the Repair and Replacement Account for prior capital improvements. The mode for Junior Lien Revenue Bonds or any portion thereof may be converted to a different mode, or to an auction rate with an interest rate period of different duration, at the direction of the City. Following such a conversion, the Junior Lien Revenue Bonds or portion thereof, will bear interest at the corresponding daily rate, weekly rate auction rate, commercial paper rate, term rate, or fixed rate.

In June 2003, CPS entered into a Forward Delivery Bond Purchase Agreement to issue \$350,500 of New Series 2003 Refunding Bonds in November 2003. The bonds sold at a premium of \$37,600 were issued to refund \$375,500 of 1994-A New Series Bonds. The refunding transaction resulted in cash flow savings of \$32,900, which equated to a present value savings of \$24,000, or approximately 6.4% of the par amount of refunded bonds. This transaction resulted in a loss for accounting purposes of \$10,600, which has been deferred and will be amortized over the shorter of the life of the refunded or refunding bonds.

In July 2003, CPS issued \$93,900 of New Series 2003A Revenue Refunding Bonds. The bonds were sold at a premium of \$11,000 and were issued to advance refund \$24,400 of 1994-A New Series Bonds, and \$71,600 of 1995 New Series Bonds. The refunding transaction resulted in a cash flow savings of \$15,900, which equated to a present value savings of \$5,800, or 6.1% of the par amount of the refunded bonds. This transaction resulted in a loss for accounting purposes of \$7,900, which has been deferred and will be amortized over the shorter of the life of the refunded or refunding bonds.

In November 2004, CPS issued \$160,000 of variable-rate, Junior-Lien Revenue Bonds. The bonds were issued initially in a term mode at par value. Of the proceeds, approximately \$132,500 was issued to acquire an additional 300 megawatts of electric generating capacity in STP with the remaining proceeds to be used for system improvements and to pay costs and expenses relating to the issuance of the bonds.

(amounts are expressed in thousands)

6. LONG-TERM DEBT (Continued)

B. City Public Service (CPS) (Continued)

On March 9, 2005, CPS issued \$535,300 of tax-exempt New Series 2005 Bonds. Included were par amounts of \$294,600 of Revenue Refunding Bonds and \$240,700 of Revenue Bonds. The true interest cost of these bonds was approximately 4.5%. CPS expects to receive net proceeds of \$250,000 from the issuance of the Revenue Bonds. Proceeds will be used to partially fund Transmission, Electric Distribution, Information Technology & Communication, and General Property construction. The bonds to be refunded are expected to result in net present value ("NPV") debt service savings of \$19,700, or approximately 6.7% of the par amount of the refunded bonds. Closing of the bond transaction is scheduled for April 13, 2005.

	Long-Term Debt Activity					
	Issue	Original Amount	Final Principal Payment	Interest Rates (%)	Balance Outstanding February 1, 2004	Balance Outstanding January 31, 2005
Revenue and Refunding Bonds						
1992 Tax-exempt		\$ 700,805	2006	6.048	\$ 68,860	\$ 36,875
1994-A Tax-exempt		684,700	2012	5.008	68,965	68,965
1994-C Tax-exempt		56,000	2006	5.008	42,710	42,710
1995 Tax-exempt		125,000	2007	5.500	14,800	11,300
1997 Tax-exempt		350,000	2020	5.738	169,715	169,715
1997 Tax-exempt		311,170	2014	5.509	103,055	102,715
1998A Tax-exempt		785,515	2021	4.918	619,030	582,965
1998B Taxable		99,615	2020	6.343	91,815	89,870
2000A Tax-exempt		170,770	2010	5.374	19,465	15,795
2000B Taxable		50,425	2021	7.403	46,495	45,010
2001 Tax-exempt		115,280	2011	3.843	106,430	106,430
2002 Tax-exempt		436,090	2017	4.055	436,090	436,090
2002 Tax-exempt		140,615	2020	4.751	140,615	140,615
2003 Tax-exempt Junior Lien		250,000	2033	Variable	250,000	250,000
2003A Tax-exempt		93,935	2014	3.675	93,935	89,770
2003 Tax-exempt		350,490	2013	3.081	350,490	312,400
2004 Tax-exempt Junior Lien		160,000	2027	Variable		160,000
					2,622,470	2,661,225
Less Bond current maturities					121,245	127,255
Less Bond discount/(premium)					(103,956)	(89,149)
Less Bond acquisition costs						24,494
Revenue Bonds, Net						2,488,892
Tax-Exempt Commercial Paper (TECP)					153,990	111,558
Long-term Debt, Net					\$ 153,990	\$ 2,838,892

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(amounts are expressed in thousands)

6. LONG-TERM DEBT (Continued)

C. San Antonio Water System (SAWS)

On April 30, 1992, City Ordinance No. 75686 was adopted. This ordinance authorized the issuance of \$635,925 Water System Revenue Refunding Bonds, Series 1992, dated April 15, 1992. These bonds were issued to refund in advance of maturity \$253,065 Water Revenue Bonds authorized and outstanding under terms of City Ordinance No. 52091, \$330,125 of Sewer Revenue Bonds authorized and outstanding under terms of City Ordinance No. 51975, \$14,500 of other bonded debt of annexed water districts, and \$49,200 of Sewer System Commercial Paper. The purpose of this advance refunding was to release and discharge the covenants contained in City Ordinance No. 52091 and No. 51975 in order to permit the City to consolidate the operations of the water-related utilities.

The System – City Ordinance No. 75686 defines SAWS as all properties, facilities, plants owned, operated and maintained by the City and/or the Board of Trustees, for the supply, treatment, transmission, and distribution of treated potable water, chilled water and steam, for the collection and treatment of wastewater and for water reuse, together with all future extensions, improvements, purchases, repairs, replacements and additions thereto, and any other projects and programs of SAWS; however, the City retains the right to incorporate a stormwater system as provided by the Texas Local Government Code. See “Stormwater” below.

Funds Flow – City Ordinance No. 75686 requires that Gross Revenues of SAWS be applied in sequence to: (1) current maintenance and operating expenses including a two-month reserve based upon the budgeted amount of maintenance and operating expenses for the current fiscal year; (2) Debt Service Fund requirements of Senior Lien Obligations; (3) Reserve Fund requirements of Senior Lien Obligations; (4) Interest and Sinking Fund and Reserve Fund requirements of Junior Lien Obligations; (5) Interest and Sinking Fund and Reserve Fund requirements of Subordinate Lien Obligations; (6) Payment of amounts required on Junior Lien Obligations; and (7) Transfers to the City’s General Fund and to the Renewal and Replacement Fund.

Reuse Contract – SAWS has a contract with City Public Service, the City owned electricity and gas utility, for the provision of reuse water. The revenues derived from the contract have been restricted in use to only reuse activities, and are excluded from the calculation of Gross Revenues, and are not included in any transfers to the City’s General Fund. Revenues derived from this contract were \$2,167 during the twelve months ended December 31, 2004.

SAWS is developing a recycled water system that will provide non-potable water to various customers now using Edwards Aquifer water. During the twelve months ended December 31, 2004, SAWS generated an additional \$2,669 in revenue from sales of recycled water. Revenue from recycled water sales is recorded as revenue of SAWS and has the same restrictions as the reuse contract.

Stormwater – In addition to the water related utilities which the Board has under its control, the City Council approved Ordinance No. 77949 on May 13, 1993, which established initial responsibilities over the Stormwater Program with the System and adopts a schedule of rates to be charged for stormwater services and programs. The Stormwater Program is deemed to not be a part of SAWS as the term is defined in City Ordinance No. 75686. Accordingly, operations of the Stormwater Program are not considered when determining compliance with debt covenants contained in City Ordinance 75686 or in calculating payments to be made to the City. In fiscal year 1997, the City Council placed the administrative responsibility with its own staff and entered into an interlocal agreement with SAWS for the provision of services related to certain water quality monitoring functions.

No Free Service – City Ordinance No. 75686 also provides for no free services except for municipal fire-fighting purposes.

(amounts are expressed in thousands)

6. LONG-TERM DEBT (Continued)

C. San Antonio Water System (SAWS) (Continued)

Revenue Bonds

On June 30, 2004, SAWS issued \$84,700 City of San Antonio, Texas Water System Revenue and Refunding Bonds, Series 2004. The proceeds from the sale of the Bonds were used to (i) provide funds for the purpose of acquiring, purchasing, constructing, improving, renovating, enlarging, and equipping SAWS, (ii) refund \$5,000 in outstanding commercial paper notes, and (iii) pay the cost of issuing the bonds. The bonds are secured together with other outstanding Senior Lien Obligations solely by a lien on and pledge of net revenues.

On July 7, 2004, SAWS issued \$10,635 City of San Antonio, Texas Water System Junior Lien Revenue and Refunding Bonds, Series 2004 with the Texas Water Development Board. The Bonds were sold under the Federal Cross Cutter Program with interest rates ranging from 0.00% - 3.20%. The proceeds from the sale of the bonds were used to (i) finance capital improvement projects which qualify under the Texas Water Development Board Program (ii) refund \$4,800 in outstanding commercial paper notes, and (iii) pay the cost of issuance. The bonds are secured together with other currently outstanding Junior Lien Obligations solely by a lien on a pledge of net revenues and are subordinate of outstanding Senior Lien Obligations.

On July 7, 2004, SAWS issued \$26,365 City of San Antonio, Texas Water System Junior Lien Revenue and Refunding Bonds, Series 2004-A with the Texas Water Development Board. The bonds were sold under the State Revolving Fund (SRF) Program, with interest rates ranging from 0.75% - 4.20%. The proceeds from the sale of the bonds were used to (i) finance capital improvement projects which qualify under the Texas Water Development Board Program, (ii) refund \$20,800 in outstanding commercial paper notes, and (iii) pay the cost of issuance. The bonds are secured together with other currently outstanding Junior Lien Obligations solely by a lien on a pledge of net revenues and are subordinate to outstanding Senior Lien Obligations.

All three issues resulted in the conversion of debt from short-term to long-term. As a result, there was no economic gain or loss associated with the refunding.

Senior Lien Water System Revenue Bonds, comprised of Series 1996, Series 1997, Series 1999, Series 2001, Series 2002, Series 2002-A, and Series 2004, outstanding in the amounts of \$822,860 at December 31, 2004, are collateralized by a senior lien and pledge of the Gross Revenues of SAWS after deducting and paying the current expenses of operation and maintenance of SAWS and maintaining an operating reserve for operating and maintenance expenses. At December 31, 2004, these bonds are due in varying amounts, from a low of \$5,275 in 2033 to a high of \$62,485 in 2028.

Junior Lien Water System Revenue Bonds, comprised of Series 1999, Series 1999-A, Series 2001, Series 2001-A, Series 2002, Series 2002-A, Series 2003, Series 2004, and Series 2004-A outstanding in the amount of \$219,035 at December 31, 2004, are collateralized by a junior lien and pledge of the Gross Revenues of SAWS after deducting and paying the current expenses of operation and maintenance of SAWS maintaining an operating reserve for operating and maintenance expenses, and debt service on senior lien debt. At December 31, 2004, the Junior Lien bonds are due in varying amounts, from a low of \$3,120 in 2024 to a high of \$17,885 in 2019.

Subordinate Lien Water System Revenue Bonds, comprised of Series 2003-A and 2003-B, outstanding in the amount of \$120,515 at December 31, 2004, are collateralized by a subordinate lien and pledge of the Gross Revenues of SAWS after deducting and paying the current expenses of operation and maintenance of SAWS maintaining an operating reserve for operating and maintenance expenses, and debt service on senior lien and junior lien debt. At December 31, 2004, the Subordinate Lien bonds are due in varying amounts, from a low of \$2,080 in 2005 to a high of \$7,240 in 2033.

(amounts are expressed in thousands)

6. LONG-TERM DEBT (Continued)

C. San Antonio Water System (SAWS) (Continued)

Revenue Bonds (Continued)

Revenue bonds currently outstanding are as follows:

San Antonio Water System					
Purpose	Interest Rates	Amount			
Build, improve, extend, enlarge, and repair the System	0.00-6.25%	\$ 1,162,410			
The following summarizes transactions of the revenue bonds for the year ended December 31, 2004:					
	Beginning Balance Jan. 1, 2004	Additions	Reductions	Ending Balance Dec. 31, 2004	Due Within One Year
Bonds Payable	\$ 1,048,445	\$ 121,700	\$ 7,735	\$ 1,162,410	\$ 16,505
Deferred Amounts					
For issuance discounts/ premiums/losses	(29,802)		1,771	\$ (28,031)	
Total Bonds Payable, net	\$ 1,018,643	\$ 121,700	\$ 9,506	\$ 1,134,379	\$ 16,505

Annual debt service requirements are shown as follows:

San Antonio Water System					
Annual Debt Service Requirements					
Revenue Bonds					
Year Ended December 31,	Subordinate Lien Revenue and Refunding Bonds		Junior Lien Revenue and Refunding Bonds		Senior Lien Revenue and Refunding Bonds
	Principal	Interest	Principal	Interest	Principal
2005	\$ 2,080	\$ 5,037	\$ 4,945	\$ 7,407	\$ 9,480
2006	2,170	4,951	5,100	7,247	15,145
2007	2,275	4,860	7,850	7,044	14,755
2008	2,375	4,765	8,085	6,796	18,705
2009	2,485	4,665	10,285	6,520	19,585
2010-2014	14,235	21,671	67,130	26,782	105,095
2015-2019	17,780	18,413	80,430	14,047	132,650
2020-2024	22,220	14,343	35,210	2,598	216,980
2025-2029	27,770	9,255			240,050
2030-2034	27,125	2,897			50,415
Total	\$ 120,515	\$ 90,857	\$ 219,035	\$ 78,441	\$ 822,860
					\$ 686,820

(amounts are expressed in thousands)

6. LONG-TERM DEBT (Continued)

C. San Antonio Water System (SAWS) (Continued)

Capitalized Interest Costs

Interest costs incurred on revenue bonds and short-term commercial paper debt totaled \$55,851 during the twelve months ended December 31, 2004, of which \$15,918 was capitalized as part of the cost of SAWS' utility plant additions.

Leases

SAWS entered into various lease agreements for financing the acquisition of computer equipment and heavy equipment. These lease agreements meet the requirements of capital leases for accounting purposes and, therefore, are recorded at the present value of the future minimum lease payments as of the inception date. The annual percentage rate of the leases ranges from 5.5% to 7.5%. At the end of the respective lease terms, the ownership of the equipment transfers to SAWS or SAWS has the option to purchase the equipment. SAWS recorded capital leases related to computer equipment and heavy equipment in the amount of \$273.

The future minimum lease obligations as of December 31, 2004, are as follows:

San Antonio Water System			
Minimum Lease Obligation			
Year Ending December 31	Principal	Interest	Total Annual Requirements
2005	\$ 265	\$ 11	\$ 276
2006	8		8
Total	\$ 273	\$ 11	\$ 284

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6. LONG-TERM DEBT (Continued)

(amounts are expressed in thousands)

6. LONG-TERM DEBT (Continued)

C. San Antonio Water System (SAWS) (Continued)

Note Payable

During fiscal year 2000, a contract was entered into between SAWS and CPS whereby SAWS acquired water rights from certain CPS properties. A note was signed for 116 payments of \$40 at an interest rate of 7.5%. Total payments on this note are \$4,640 including interest. The liability as of December 31, 2004, is included in the statement of net assets for both the current portion of \$362 and long-term amount of \$1,380. The annual principal and interest requirements are as follows:

San Antonio Water System Principal and Interest Requirements				
Year Ending December 31	Principal	Interest	Total Annual Requirements	
2005	\$ 362	\$ 118	\$	480
2006	390	90		480
2007	420	60		480
2008	452	28		480
2009	118	2		120
Total	\$ 1,742	\$ 298	\$	2,040

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(amounts are expressed in thousands)

7. COMMERCIAL PAPER PROGRAMS AND OTHER BORROWINGS

A. Primary Government (City)

Revolving Line of Credit

The City uses a revolving line of credit for the Housing Asset Recovery Program. The line of credit is used to preserve housing stock and to revitalize neighborhoods by renovating and rehabilitating property owned by the City that is acquired through various programs (i.e. flood buyouts, facilities expansion, etc.). The City intends to finance their repayment with the proceeds received from the sale of the renovated houses. The amount of the line of credit is \$1,250, of which \$301 was outstanding as of September 30, 2005.

Revolving Line of Credit			
Beginning Balance	Increases	Decreases	Ending Balance
\$ 301	\$ -	\$ -	\$ 301

B. City Public Service (CPS)

Commercial Paper

In 1988, the City Council adopted an ordinance authorizing the issuance of up to \$300,000 in Tax-Exempt Commercial Paper (TECP). This ordinance, as amended in June 1997, provides for funding to assist in the financing of eligible projects, in an aggregate amount not to exceed \$450,000. Eligible projects include fuel acquisition, capital improvements to the utility systems (the Systems), and refinancing or refunding any outstanding obligations that are secured by and payable from a lien on and/or a pledge of net revenues of the Systems. The program's scheduled maximum maturities will not extend beyond November 1, 2028.

The TECP has been classified as long-term in accordance with the refinancing terms under a revolving credit agreement with a consortium of banks, which supports the commercial paper. Under the terms of the agreement, CPS may borrow up to an aggregate amount not to exceed \$350,000 for the purpose of paying principal due under the TECP. The credit agreement has a term of two years, currently extended until November 1, 2007, and may be renewed for additional periods.

To date, there have been no borrowings under the credit agreement. The TECP is secured by the net revenues of the Systems. Such pledge of net revenues is subordinate and inferior to the pledge securing payment of existing New Series Bonds and any to be issued in the future.

As of January 31, 2005, a summary of TECP is as follows:

TECP Outstanding	\$	350,000
Weighted-average interest rate of outstanding TECP, approximate		0.90%
Average life of outstanding TECP (approximate number of days)		70

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(amounts are expressed in thousands)

7. COMMERCIAL PAPER PROGRAMS AND OTHER BORROWINGS (Continued)

C. San Antonio Water System (SAWS)

Commercial Paper

SAWS maintains a Commercial Paper Program that is used to provide funds for the interim financing of a portion of capital improvements to the System.

On January 11, 2001, the City Council approved the expansion of the TECP Program (Tax Exempt Commercial Paper) from \$175,000 to \$350,000. The increase in the program provides interim financing for the increased level of future expenditures on water resource projects. Notes payable under the program cannot exceed maturities of 270 days and scheduled maturities of the short-term borrowing under the Commercial Paper Program may not extend past May 14, 2032.

The City has covenanted in the ordinance authorizing the Commercial Paper Program (the "Note Ordinance") to maintain at all times credit facilities with banks or other financial institutions that would provide available borrowing sufficient to pay the principal of the Commercial Paper Program. The credit facility is maintained under the terms of a revolving credit agreement.

To further support the issuance of the Commercial Paper Program, on June 2, 2001, the City entered into the agreements with the following participants:

- Dealer Agreements with Goldman, Sachs & Co., J.P. Morgan Securities Inc., and Ramirez & Co., Inc.
- Revolving Credit Agreement with Bank of America, N.A.
- Issuing and Paying Agency Agreement with Bank One, National Association Chicago, Illinois.

The borrowings under the Commercial Paper Program are equally and ratably secured by and are payable from (i) the proceeds from the sale of bonds or additional borrowing under the Commercial Paper Program and (ii) borrowing under and pursuant to the revolving credit agreement.

Commercial paper notes of \$238,400 are outstanding as of December 31, 2004. The proceeds of the notes have been used solely for financing of capital improvements of SAWS. The tax-exempt commercial paper notes have been classified as long-term in accordance with the refinancing terms of the Credit Agreement, and since management intends to continue the remarketing of the tax-exempt commercial paper notes to maintain a portion of its debt in variable rates. Interest rates on the notes outstanding at year-end range from 1.7% to 1.9% and from 34 to 96 days in maturity. (The outstanding notes at December 31, 2004, had an average rate of 1.8% and averaged 67 days to maturity.)

The following summarizes transactions of the commercial paper program for the year ended December 31, 2004.

	Beginning Balance	Ending Balance		Due Within One Year
		Jan. 1, 2004	Dec. 31, 2004	
Commercial Paper Notes	\$ 269,000	\$ -	\$ 30,600	\$ -

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(amounts are expressed in thousands)

8. PENSION AND RETIREMENT PLANS

A. General Plan Information

The City of San Antonio, SAWS, and CPS participate in several contributory retirement plans. These are funded plans covering substantially all full-time employees. Payroll and contribution information as of the year-end for each entity is presented below:

Contributory Pension and Retirement Plans						
Entity	Title	Type of Plan	Covered Payroll	Employee Contribution	Employer Contribution	Total Contributions
City	Fire and Police Pension Fund	Single Employer Defined Benefit Plan	\$ 200,904	\$ 24,896	\$ 49,665	\$ 74,561
	Texas Municipal Retirement System (TMRS)	Non Traditional Hybrid Defined Benefit Agent Plan	\$ 205,876	\$ 12,325	\$ 25,131	\$ 37,456
Component Units:						
SAWS	¹ Texas Municipal Retirement System (TMRS)	Non Traditional Defined Contribution Agent Plan	Not Available	\$ 1,830	\$ 2,013	\$ 3,843
	² PMLJC Contract	Agent Multiple Employer Defined Benefit Plan	\$ 56,932	\$ -	\$ 3,486	\$ 3,486
CPS	³ CPS All Employees Plan	Single Employer Defined Benefit Plan	\$ 189,892	\$ 9,215	\$ 8,160	\$ 17,375

¹ Plan year ended December 31, 2004

² Plan year ended December 31, 2004

³ Fiscal year ended January 31, 2005

¹ Plan year ended December 31, 2004

² Plan year ended December 31, 2004

³ Fiscal year ended January 31, 2005

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(amounts are expressed in thousands)

8. PENSION AND RETIREMENT PLANS (Continued)

B. Primary Government (City)

Fire and Police Pension Plan

The Pension Fund is a single-employer defined benefit retirement plan established in accordance with the laws of the State of Texas. The City provides retirement benefits for all eligible full-time Fire and Police employees through the Pension Fund. Employees who terminate, having five to twenty years of service, may apply to receive a refund of their original contribution. Employees retiring who have served and contributed for twenty years or more shall, upon application to the Board of Trustees of the Pension Fund, receive a retirement pension based on the average of the employee's total salary, excluding overtime pay, for the highest three years of pay of the last five years of service. The retirement annuity for employees retiring after September 30, 2003, is computed at the rate of 2.3% of this average for each of the first twenty years of service, plus 4.5% of the member's average total salary for each of the next seven years, plus 3.0% of the member's average total salary for each of the next three years of service, plus 0.5% of the member's average total salary for each of the next four years of service, with fractional years of service prorated based on full months served as a contributing member. In applying the computation for a year, the year is considered to begin on the first day a contribution is made. A retirement annuity under this subsection may not exceed, as of the date of retirement, 87.5% of the member's average total salary.

An employee with twenty years and one month of actual service credit, may at the time of retirement elect a Backward Deferred Retirement Option Plan (Back DROP). The Back DROP election results in a lump sum payment equal to the number of full months of service elected by an employee that does not exceed the lesser of the number of months of service credit the employee had in excess of twenty years or thirty-six months and a reduced annuity payment.

There is also a provision for a thirteenth and fourteenth pension check. The Board may authorize the disbursement of a thirteenth monthly pension check if the yield on the Pension Fund's investments exceeds the actuarial projections for the preceding five year period by at least 100 basis points. The Board may authorize a fourteenth monthly pension check if the yield on the Pension Fund's investments exceeds the actuarial projections for the preceding five-year period by at least 300 basis points. The thirteenth and fourteenth pension checks are paid to each retiree and beneficiary receiving a pension at the time of the disbursement and are in an amount equal to the pension check paid in the last month of the preceding fiscal year of the Pension Fund (retirees/beneficiaries with less than one year of benefits will receive a prorated check, and no check will be paid to members who retired after the end of the fiscal year).

If service is terminated by reason of death or disability, the employee's beneficiary or the employee shall be entitled to one-half of the average of the employee's total salary, excluding overtime pay, based on the same number of years of the member's pay as used to compute normal retirement benefits. If a member is killed in the line of duty, the member's surviving spouse and dependent children are entitled to a pension based upon actual base salary at time of death.

The Pension Fund issues a publicly available financial report that includes financial statements and required supplemental information. That report may be obtained by writing to the Fire and Police Pension Fund of San Antonio, 311 Roosevelt, San Antonio, Texas 78210-2700 or by calling (210) 534-3262.

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(amounts are expressed in thousands)

8. PENSION AND RETIREMENT PLANS (Continued)

B. Primary Government (City) (Continued)

Fire and Police Pension Plan (Continued)

Contribution requirements of plan members and the City are established and may be amended by State statute. In the current year, the City contributed 24.64% of covered payroll, and employees contributed 12.32% of covered payroll. The employer's required contribution of \$49,665 and the employee's required contribution of \$24,896 were made to the Pension Fund. (See summary of contribution information at Part A of this footnote). New fire fighters and police officers are immediately eligible for membership after they receive state certification and complete all other requirements. For the fiscal year ended September 30, 2005, the City does not begin matching contributions until the member has completed the probationary period (currently two months after a member becomes eligible). The City will match the contributions of new fire fighters and police officers during the probationary period beginning October 1, 2005.

Effective October 1, 2001, in addition to the changes for credited service and the fourteenth check as mentioned previously, other new provisions include allowing the surviving spouse of an active member to elect to receive benefits in the form of a lump-sum payment and reduced annuity, similar to a Back DROP election made by a retiring member, increasing the maximum benefit for surviving spouses and dependent children equal to a 27-year pension, and increasing cost-of-living increases for all retirees who retired between August 30, 1971 and October 1, 1991.

Another important provision of the Pension Fund is the Cost of Living Adjustment (COLA). The COLA is based on the Consumer Price Index for all Urban Consumers - U.S. City Average (CPI) as published by the Bureau of Labor Statistics. Members whose retirement, disability, or death occurred before August 30, 1971, received an increase equal to 100.0% of the increase in the CPI. Members whose retirement, disability, or death occurred after August 30, 1971, but before October 1, 1991, receive an increase equal to 100.0% of the increase in the CPI up to 8.0%, and 75.0% of the increase in the CPI in excess of 8.0%. Members whose retirement, disability, or death occurred after October 1, 1991, receive an increase equal to 75.0% of the increase in the CPI.

The Pension Fund's governing statute was amended by the Texas Legislature effective October 1, 2005. The major changes enacted during the 2005 legislative session are (i) administrative changes to permit the Board to operate more efficiently, (ii) providing for an election to be made by a service retiree to receive a reduced annuity during the retiree's lifetime to provide a death benefit annuity to the retiree's post-retirement surviving spouse, (iii) providing for an increased death benefit payment by the Fund to an active member's or retiree's estate if there is no named beneficiary, (iv) changing the threshold year for determining increases in annuities based on CPI increases from 1991 to 1993, (v) allowing the use of a participant's salary beyond 34 years of service for purposes of a Back DROP benefit calculation, and (vi) increasing the service allowed in determining the spouse Back DROP lump-sum from 27 to 30 years.

Texas Municipal Retirement System (TMRS)

The City provides benefits for all eligible employees (excluding firefighters and police officers) through a nontraditional, joint contributory, hybrid defined benefit plan in the TMRS. The TMRS is a statewide agent multiple-employer public employee retirement system created by law in 1948 to provide retirement and disability benefits to city employees. It is the opinion of the TMRS management that the plans in TMRS are substantially defined benefit plans, but they have elected to provide additional voluntary disclosure to help foster a better understanding of some of the nontraditional characteristics of the plan.

TMRS issues a publicly available financial report that includes financial information related to participating municipalities. The report may be obtained by writing to the TMRS, P.O. Box 149153, Austin, Texas 78714-9153 or calling (512) 476-7577.

(amounts are expressed in thousands)

8. PENSION AND RETIREMENT PLANS (Continued)

B. Primary Government (City) (Continued)

Texas Municipal Retirement System (TMRS) (Continued)

Benefits depend upon the sum of the employee's contributions to the plan, with interest, and the City-financed monetary credits, with interest. At the date the plan began, the City granted monetary credits for service rendered before the plan began of a theoretical amount equal to two times what would have been contributed by the employee, with interest, prior to establishment of the plan. Monetary credits for service since the plan began are a percentage of the employee's accumulated contributions. In addition, the City may grant, as often as annually, another type of monetary credit referred to as an updated service credit. This is a theoretical amount which, when added to the employee's accumulated contributions and the monetary credits for service since the plan began, would be the total monetary credits and employee contributions accumulated with interest if the current employee contribution rate and City matching percent had always been in existence and if the employee's salary had always been the average salary for the last three years. At retirement, the benefit is calculated as if the sum of the employee's accumulated contributions with interest and the City-financed monetary credits with interest were used to purchase an annuity.

Members are eligible to retire upon attaining the normal retirement age of 60 and above with five or more years of service or with 20 years of service regardless of age. The plan also provides death and disability benefits. A member is vested after five years, but must leave accumulated contributions in the plan. If a member withdraws the contributions with interest, the member would not be entitled to the City-financed monetary credits, even if vested.

The plan provisions and contribution requirements are adopted by the governing body of the City within the options available in the state statutes governing TMRS and within the actuarial constraints contained in the statutes.

Contribution requirements are actuarially determined by TMRS' actuary (See summary of TMRS Actuarial Assumptions and Methods in Part F of this footnote). The contribution rate for the City's employees is 6.0% and the matching percent is currently 12.5%, both as adopted by the governing body of the City. (See summary of contribution information in Part A of this footnote.) Under the state law governing TMRS, the Employer's Contribution rates are annually determined by the actuary. This rate consists of the normal cost contribution rate and the prior service contribution rate, both of which are calculated to be a level percent of payroll from year to year. The normal cost contribution finances the currently accruing monetary credits due to the City matching percent, which are the obligation of the City as of an employee's retirement date, not at the time the employee's contributions are made. The normal cost contribution rate is the actuarially determined percent of payroll necessary to satisfy the obligation of the City to each employee at the time the employee's retirement becomes effective. The prior service contribution rate amortizes the unfunded actuarial liability over the remainder of the plan's twenty-five year amortization period. When the City periodically adopts updated service credits and increases annuities in effect, the increased unfunded actuarial liability is being amortized over a new twenty-five year period. Currently, the unfunded actuarial liability is amortized over a constant twenty-five year period as a level percent of payroll. Contributions are made monthly by both the employees and the City. All current year required contributions of the employees and the City were made to TMRS. Due to the fact that the City requires the contribution rates in advance for budget purposes, there is a one-year lag between the actuarial valuation that is the basis for the rate and the calendar year when the rate goes into effect.

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(amounts are expressed in thousands)

8. PENSION AND RETIREMENT PLANS (Continued)

C. San Antonio Water System (SAWS)

SAWS' retirement program includes benefits provided by the Texas Municipal Retirement System, a contract with Principal Mutual Life Insurance Company, and Social Security.

Covered employees are eligible to retire upon attaining the normal retirement age of 65. An employee may elect early retirement, with reduced benefits, upon attainment of:

1. 20 Years of credited service regardless of age, or
2. 25 Years of credited service and at least age 50, or
3. 10 Years of credited service and at least age 60.

The normal retirement benefit is based upon two factors, average compensation and years of credited service. Average Compensation is defined as the monthly average of total compensation received for the three consecutive years ending December 31, out of the latest ten compensation years prior to normal retirement date which gives the highest average.

The normal retirement benefit under the Principal Mutual contract is equal to:

1. 1.2% of the Average Compensation, times years of credited service not in excess of 25 years, plus
2. 0.75% of the Average Compensation, times years of credited service in excess of 25 years but not in excess of 35 years, plus
3. 0.375% of the Average Compensation, times years of credited service in excess of 35 years.

Upon retirement, an employee must select from one of seven alternative payment plans. Each payment plan provides for monthly payments as long as the retired employee lives. The options available address how plan benefits are to be distributed to the designated beneficiary of the retired employee. The program also provides death and disability benefits. The following information related to the Texas Municipal Retirement System and Principal Mutual Life Insurance has been prepared as of January 1, 2004.

Texas Municipal Retirement System (TMRS)

SAWS provides pension benefits for all of its full-time employees through a nontraditional, joint contributory, defined benefit plan in the Texas Municipal Retirement System (TMRS), an agent multiple-employer public employee retirement system. The TMRS was established in 1948 as a retirement and disability pension system for municipal employees in the State of Texas, and is administered in accordance with the Texas Municipal Retirement System Act. It is the opinion of the TMRS management that the plans in the TMRS are substantially defined benefit plans, but they have elected to provide additional voluntary disclosure to help foster a better understanding of some of the nontraditional characteristics of the plan.

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(amounts are expressed in thousands)

8. PENSION AND RETIREMENT PLANS (Continued)

C. San Antonio Water System (SAWS) (Continued)

Texas Municipal Retirement System (TMRS) (Continued)

Benefits depend upon the sum of the employee's contributions to the plan, with interest, and the SAWS-financed monetary credits, with interest. At the date the plan began, SAWS granted monetary credits for service rendered before the plan began of a theoretical amount equal to two times what would have been contributed by the employee, with interest, prior to establishment of the plan. Monetary credits for service since the plan began are a percent (100.0%, 150.0%, and 200.0%) of the employee's accumulated contributions. In addition, SAWS may grant, as often as annually, another type of monetary credit referred to as an updated service credit which is a theoretical amount which, when added to the employee's accumulated contributions and the monetary credits for service since the plan began, would be the total monetary credits and employee contributions accumulated with interest if the current employee contribution rate and SAWS matching percent had always been in existence and if the employee's salary had always been the average salary for the last three years that are one year before the effective date. At retirement, the benefit is calculated as if the sum of the employee's accumulated contributions, with interest, and the employer-financed monetary credits, with interest, were used to purchase an annuity.

Members can retire at age 60 and above with five or more years of service or with 20 years of service regardless of age. A member is vested after five years. The plan provisions and contribution requirements are adopted by SAWS within the options available in the state statutes governing TMRS and within the actuarial constraints contained also in the statutes.

Contribution requirements are actuarially determined by TMRS' actuary (see Summary of TMRS' Actuarial Assumptions and Methods in Part F of this footnote). The contribution rate for the employees is 3.0% of salary, and SAWS matching rate approximates 100.0% of the employee rate, both as adopted by the SAWS. Under the state law governing TMRS, SAWS' contribution rate is annually determined by the actuary. This rate consists of the normal cost contribution rate and the prior service cost contribution rate, both of which are calculated to be a level percent of payroll from year to year. The normal cost contribution rate finances the currently accruing monetary credits due to SAWS' matching percent, which are the obligation of SAWS as of an employee's retirement date, not at the time the employee's contributions are made. The normal cost contribution rate is the actuarially determined percent of payroll necessary to satisfy the obligation of SAWS to each employee at the time his/her retirement becomes effective. The prior service contribution rate amortizes the unfunded (overfunded) actuarial liability (asset) over the remainder of the plan's 25-year amortization period.

When SAWS periodically adopts updated service credits and increases the annuities in effect, the increased unfunded actuarial liability is to be amortized over a new twenty-five year period. Currently, the unfunded actuarial liability is to be amortized over the twenty-five year period. The unit credit actuarial cost method is used for determining SAWS contribution rate.

Contributions are made monthly by both the employees and SAWS. Since SAWS needs to know its contribution rate in advance for budgetary purposes, there is a one-year delay between the actuarial valuation that is the basis for the rate and the calendar year when the rate goes into effect. Significant assumptions used in the actuarial valuation of annual required contributions include a rate of return on the investment of present and future assets of 8.0% per year. Additionally, there is no need to project salary increases since the benefit credits earned for service to date are not dependent on future salaries. Likewise, inflation and cost-of-living adjustments are not accounted for in the actuarial study. Assets are valued at amortized cost.

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(amounts are expressed in thousands)

8. PENSION AND RETIREMENT PLANS (Continued)

C. San Antonio Water System (SAWS) (Continued)

Principal Mutual Life Insurance Company

The contract with Principal Mutual Life Insurance Company (PMLIC) serves as a supplement to the TMRS and Social Security benefits. SAWS' covered payroll at January 1, 2004, under this contract was \$56,932.

SAWS provides supplemental pension benefits for all persons customarily employed at least 20 hours per week and five months per year through this defined benefit plan. Employees are eligible to participate in the plan on January 1 of the calendar year following date of hire. An employee covered by the plan may vest a portion of the plan benefits if termination occurs after sufficient years of service have been credited. The plan allows an employee to accrue vesting benefits as follows:

Years of Service	Vested Percentage
Less than 5	0%
5	50%
6	60%
7	70%
8	80%
9	90%
10 or more	100%

An employee is automatically 100.0% vested upon attainment of age 65 or upon becoming totally and permanently disabled.

Benefits for retired employees are fully guaranteed at retirement. The pension plans unallocated insurance contracts are valued at contract value. Contract value represents contributions made under the contract, plus interest at the contract rate, less funds used to purchase annuities or pay administrative expenses charged by Principal Life Insurance Co. The plan provisions and contribution requirements are governed by SAWS, which may amend plan provisions and is responsible for the management of plan assets.

Significant assumptions used by PMLIC's actuary to compute the actuarially determined contribution requirements include: (a) a rate of return on the investment of present and future assets of 8.3% per year, and (b) a salary scale from Table S-5 of the Actuary's Pension Handbook, plus 3.4%.

The PMLIC contract funding policy provides for actuarially determined periodic contributions so that sufficient assets will be available to pay benefits when due. The actuarial cost method is known as the Entry Age Normal-Frozen Initial Liability Method. This method spreads the total cost of the projected pension benefits for each employee evenly from the date the employee is first eligible for the plan to the employee's assumed retirement date. As plan benefits are related to compensation, the cost is spread as a level percentage of compensation. The total of annual amounts for all employees combined is called the Normal Cost. The employee's Entry Age is determined as if the plan had always been in existence. Thus, as of the plan effective date, there are some accumulated Normal Costs for past years that have not been paid. The value of these costs is called the Frozen Initial Liability.

In subsequent years, the Frozen Initial Liability is reduced by employer deposits to the plan in excess of employer Normal Cost and interest requirements. This reduced amount is known as the Unfunded Frozen Initial Liability. Contribution requirements are established and may be amended by SAWS. Active members are not required to contribute to the plan. Any obligation with respect to the pension plan shall be paid by SAWS. The actuarial valuation, which was performed for the plan year ended December 31, 2003, reflects an unfunded frozen initial liability of \$10,643.

(amounts are expressed in thousands)

8. PENSION AND RETIREMENT PLANS (Continued)

C. San Antonio Water System (SAWS) (Continued)

Principal Mutual Life Insurance Company (Continued)

The PMLIC issues a publicly available financial report that includes financial statements and required supplemental information. That report may be obtained by writing to Principal Life Insurance Company, Pension Diversified Retirement Services, Des Moines, Iowa 50392-0001 or by calling (515) 247-5111.

D. City Public Service (CPS)

All Employee Plan

The CPS Pension Plan is a self-administered, single-employer, defined-benefit contributory pension plan (Plan) covering substantially all employees who have completed one year of service. Normal retirement is age 65; however, early retirement is available with 25 years of benefit service and to those employees who are ages 55 or older with at least 10 years of benefit service. Retirement benefits are based on length of service and compensation, and benefits are reduced for retirement before age 55 with 25 years or more of benefit service, or age 62 with less than 25 years of service.

The Plan and contribution requirements are sponsored by and may be amended by CPS, acting by and through the General Manager and Chief Executive Officer of CPS. The Plan assets are held in a separate trust that is annually audited and for which financial statements include historical trend information. Additional information may be obtained by writing the Employee Benefits Division of CPS, P.O. Box 1771, San Antonio, Texas 78296 or by calling (210) 978-2484.

Funding levels are established through annual actuarial evaluations and recommendations of an Administrative/Investment Committee, using both employee and employer contributions. Participating employees contribute 5.0% of their total compensation and are fully vested after completing seven years of credited service or at age 40. The balance of contributions made amounted to 4.3% and is the responsibility of CPS, considering actuarial information, budgetary compliance, and the need to amend the Plan with legal requirements. (See Summary of Contribution Information at Part A of this footnote.)

As calculated under GASB Statement No. 27, CPS' annual pension cost and net pension obligation for the fiscal year ended January 31, 2005, was \$8,694. The annual required contribution was determined as part of the January 1, 2004, actuarial valuation using (a) the five-year smoothed market method for asset valuation, (b) the projected unit credit for pension cost, and (c) the level dollar open for amortization. The remaining amortization period is 21.6 years and is calculated using the level dollar open amortization method.

Significant actuarial assumptions used for the January 1, 2004, actuarial valuation include (a) a rate of return on the investment of present and future assets of 8.0% per year compounded annually, (b) projected salary increases averaging 4.1%, and (c) post-retirement cost-of-living increases of 1.8%. The projected salary increases include an inflation rate of 3.5%.

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(amounts are expressed in thousands)

8. PENSION AND RETIREMENT PLANS (Continued)

E. Three-Year Trend Information

Trend information compares the annual required contribution to annual pension cost and the resultant net pension obligation as required by GASB Statement No. 27.

Pension Plan	Fiscal Year	Three-Year Trend Information					Percentage of APC Contributed
		Annual Required Contribution (ARC)	Interest on Net Pension Obligation (NPO)	Adjustment To ARC	Annual Pension Cost (APC)	Increase (Decrease) in NPO	
Fire and Police Pension-City of San Antonio	2003	\$ 45,008		\$	\$ 45,008	\$ (45,008)	100%
	2004	48,038			48,038	(48,038)	100%
	2005	49,665			49,665	(49,665)	100%
TMRS-City of San Antonio	2003	\$ 22,684		\$	\$ 22,684	\$ (22,684)	100%
	2004	23,062			23,062	(23,062)	100%
	2005	25,131			25,131	(25,131)	100%
CPS All Employees Plan ¹	2003	\$ 4,921		\$	\$ 4,921	\$ (4,921)	100%
	2004	7,651			7,651	(7,651)	100%
	2005	8,694			8,694	(8,694)	100%
TMRS-SAWS ²	2002	\$ 1,772		\$	\$ 1,772	\$ (1,772)	100%
	2003	1,905			1,905	(1,905)	100%
	2004	2,013			2,013	(2,013)	100%
PMLC-SAWS ³	2002	\$ 2,857		\$	\$ 2,857	\$ (2,857)	100%
	2003	3,324			3,324	(3,324)	100%
	2004	3,486			3,486	(3,486)	100%

1 Fiscal year ended January 31, 2005

2 Plan year ended December 31, 2004

3 Plan year ended December 31, 2004

F. Significant TMRS Actuarial Assumptions and Methods

Significant assumptions used in the actuarial valuation by the Texas Municipal Retirement System's (TMRS) actuary are provided in the table below for both the City and SAWS:

TMRS Actuarial Assumptions and Methods	
Investment Return-City	7%
Investment Return-SAWS	7%
Inflation Rate	None
Projected Salary Increases	None
Post Retirement Benefit Increases	None
Actuarial Cost Method	Unit Credit
Amortization Method	Level Percent of Payroll
Remaining Amortization Period	25 Years - Open Period
Asset Valuation Method	Amortized Cost

Location of Schedules of Funding Progress

The Schedule of Funding Progress is located in the "Required Supplementary Information" section of this report. The schedules are designed to provide information about each entity's progress in accumulating sufficient assets to pay benefits due.

(amounts are expressed in thousands)

9. POSTEMPLOYMENT RETIREMENT BENEFITS

A. Primary Government (City)

In addition to the pension benefits discussed in Note 8, the City provides all their retired employees with certain health benefits under two postemployment benefit programs. The first program is a health insurance plan, which provides benefits for all non-uniformed City retirees, and for all, pre-October 1, 1989, uniformed (fire and police) retirees. Currently, there are 6,060 active civilian employees who may become eligible in the future. Employees become eligible for the program when they reach eligibility for the TMRS Pension Plan, discussed in Note 8. At September 30, 2005, there were 1,301 retirees participating in the program that covers eligible expenses at 80% after a deductible of \$250 (single)/\$500 (family) for non-Medicare and \$125/\$250 for Medicare retirees. The cost of the program is reviewed annually, and actuarially determined costs of medical claims are funded jointly by the City and retirees on a pay-as-you-go basis shared on a targeted 67.0% City, 33.0% retiree cost allocation. Please note that the number of employees, retirees, and deductible amounts in this paragraph are not expressed in thousands. For retirees, total expenses for the year were \$9,788. For the year ended September 30, 2005, total contributions were as follows:

City	\$ 3,609
Employees	2,672
Total	<u>\$ 6,281</u>

The second postemployment benefit program of the City provides retirement health care benefits for eligible Fire and Police retirees under the Fire and Police Retiree Healthcare Fund ("Fund"). The Fund was originally established as a fund of the City pursuant to the respective Fire and Police collective bargaining agreements to provide postemployment health benefits for San Antonio Fire Fighters and Police Officers who retired on or after October 1, 1989. Effective October 1, 1997, the Fund was created as a separate and distinct statutory trust. The Fund is governed by a nine-member Board of Trustees comprised of the Mayor, two City Council members, two active police officers, two active fire fighters, a retiree representative of the Fire Department, and a retiree representative of the Police Department. The Board of Trustees is responsible for the investment of the assets of the Fund. Contribution and benefit levels are determined by the respective collective bargaining agreements with the Fire and Police Associations.

The benefits of this plan are financed on a prefunded basis. The City currently makes contributions on behalf of 3,400 active fire fighters and police officers who may be eligible for benefits under this plan in the future. The benefits of the plan are not available until the employee has completed twenty years of service, and the plan is currently providing benefits to 1,189 eligible retirees. The Program reimburses 80.0% of the amount of eligible claims for standard medical costs and 100.0% for hospitalization costs incurred by the retiree and their eligible dependents for Prefund II retirees. Please note the number of firefighters, police officers, and retirees in this section are not expressed in thousands. For the year ended September 30, 2005, total expenses for retired employees was \$13,626. Contribution levels from the current collective bargaining agreements between the City and the Fire and Police Associations, respectively, and total contributions to the Fund are summarized in the following tables. Additionally, for FY 2005, the City did not reduce its contribution to the Fund under the Fire Agreement to 8.5% of base pay plus longevity but rather maintained its contribution at 8.7 % of base plus longevity.

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(amounts are expressed in thousands)

9. POSTEMPLOYMENT RETIREMENT BENEFITS (Continued)

A. Primary Government (City) (Continued)

Fire Agreement Contribution Levels				Police Agreement Contribution Levels			
Effective Date	City % of Base Pay Plus Longevity	Firefighter Per Month		Effective Date	City % of Base Pay Plus Longevity	Police Officer Per Month	
June 1, 2002	8.92%	\$40		November 1, 2003	9.4%+\$20/member monthly	\$40	
October 1, 2002	8.71%	\$50		April 1, 2004	9.4%+\$20/member monthly	\$50	
October 1, 2003	8.51%	\$60		October 1, 2004	9.4%+\$20/member monthly	\$60	
October 1, 2004	8.33%	\$70		April 1, 2005	9.4%+\$20/member monthly	\$70	

Total Contributions to the Fund	
City	\$ 17,199
Employees and Retiree Dependent Premiums	3,264
Total Contributions	<u>\$ 20,463</u>

Historically, actuarial valuations have been performed periodically to determine the actuarial position of the Fund and whether the existing financing of the Fund can be reasonably expected to be adequate over a long period of time. Actuarial valuations over the past several years have indicated that contribution levels are not sufficient to amortize the unfunded liability. At the request of the Board of Trustees, the Fund's consulting actuaries performed an actuarial valuation dated February 14, 2005, as of October 1, 2004. The results of the actuarial valuation were that, in the opinion of the actuary, the Fund will have a long-term inadequate financing arrangement if present health benefits are left unchanged and if the monthly contributions remain at the amounts of \$60 per month for October 2004 through March 2005, and \$70 per month from April 2005 through September 2006, per active participant for police employees and \$70 per month for active fire fighters for fiscal year 2004-2005. The actuary has also recommended that the contribution be increased to 22.2% of covered payroll in addition to the continuation of the specified monthly contributions.

While the results of the studies reflect that significant changes would be required in contribution levels if benefits remain unchanged, the actuarial reports also state that the Fund does not have a short-term financing problem. As of September 30, 2005, net assets available for postemployment benefits were \$147,554, while benefits payments for the fiscal year ended September 30, 2005, were \$13,626. As noted above, contribution and benefit levels are established pursuant to the collective bargaining agreements. The current agreement with the Fire Association will expire September 30, 2005, and has an evergreen clause through September 30, 2015. This agreement was negotiated prior to the issuance of the actuarial valuation indicating that contribution levels could not sufficiently amortize the unfunded liability; however, the agreement does contain a limited re-opener related to contributions to the Fund. The City is in discussions with the Fire Association regarding the limited re-opener under the current agreement.

(amounts are expressed in thousands)

9. POSTEMPLOYMENT RETIREMENT BENEFITS (Continued)

A. Primary Government (City) (Continued)

The City approved an agreement in November of 2003 with the Police Association that will expire on September 30, 2006, and has an evergreen clause through September 30, 2016. This agreement with the Police Association increases both contributions by the City and active police officers over the term of the agreement. The agreement makes certain changes in benefits such as expanding the list of preventive services and for in-network and out-of-network pharmacy benefits with increased co-payments for drugs purchased at out-of-network pharmacies, which also became effective simultaneously under the Fire Contract. To coincide with the expiration of the City's current agreement with the Fire Association in September of 2005, the agreement with the Police Association also includes a re-opener on the benefits article in fiscal year 2005, which will allow the City to simultaneously work with both the Police and Fire Associations to continue to develop a comprehensive long-term solution for the Fund. The plan is based on a dual-track strategy of restructuring and redesigning the health benefits program and increasing City and employee contributions.

B. City Public Service (CPS)

CPS provides certain health care and life insurance benefits for retired employees. Most former CPS employees are eligible for these benefits upon retirement from CPS. Plan assets are held as part of CPS' Group Health and Life Insurance Plans and funding is from both participant and employer contributions determined by annual actuarial and in-house calculations. Retired employees contribute to the health plan in varying amounts depending upon an equity formula that considers age and years of service. The Plans may be amended by CPS. The annual cost of retiree health care and life insurance benefits funded by CPS is recognized as an expense of CPS as employer contributions are made to the programs.

These costs approximated \$4,900 for 2005. CPS reimbursed certain retirees and their spouses enrolled in Medicare Part B a percentage of the monthly premium, which totaled \$325 for fiscal year 2005.

Retired employees and covered dependents contributed \$2,200 for their health care and life insurance benefits in fiscal year 2005. There were approximately 2,386 retirees and covered dependents eligible for health care and life insurance benefits. Please note the number of retirees is not stated in thousands.

In view of the potential economic significance of these benefits, CPS has reviewed the present value of the postemployment benefit obligations for current retirees. The January 1, 2004, valuations are \$80,500 for health and \$21,800 for life insurance benefits. The actuarial analysis of the present value of postemployment benefit obligations for other participants fully eligible for benefits are estimated to be \$50,200 for health, \$6,000 for life insurance, and \$3,400 for disability benefits. CPS began partial accrual and funding of projected future benefits in 1992. Funding totaled \$5,200 in 2005. For the health care plan, the actuarial cost method used is the Projected Unit Credit Actuarial Cost Method. For the life insurance and disability plans, CPS uses a present value method to determine the cost of benefits.

Significant actuarial assumptions used in the calculations for the January 1, 2004, actuarial valuations include (a) a rate of return on the investment of present and future assets of 8.0% per year for the health, life, and disability plans, (b) projected salary increases for the plans ranging from 4.5% to 12.0% depending on age, for base and other salaries, and (c) medical cost increases projected at 9.5% for 2005-2010 decreasing to 6.0% in 2011 and thereafter.

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(amounts are expressed in thousands)

9. POSTEMPLOYMENT RETIREMENT BENEFITS (Continued)

C. San Antonio Water System (SAWS)

SAWS provides certain health care and life insurance benefits for retired employees. Substantially all full-time employees who retire from SAWS may become eligible for those benefits. On December 31, 2004, there were 468 retirees with life insurance and 480 retirees with medical coverage. Please note the numbers of retirees are not stated in thousands.

SAWS provides medical and life insurance for retirees and recognizes the cost of providing these benefits on a pay-as-you-go basis by expensing the annual insurance. Premiums for medical insurance and life insurance amounted to \$4,034 and \$76, respectively, for January 1, 2004, through December 31, 2004. Those and similar benefits for active employees are provided through insurance companies.

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(amounts are expressed in thousands)

10. CPS SOUTH TEXAS PROJECT (STP)

Joint Operations

CPS is one of four participants in the STP, which consists of two 1,250-megawatt nuclear generating units in Matagorda County, Texas. The other participants in the project are Texas Genco, L.P., formerly known as Houston Lighting & Power and Reliant Energy, American Electric Power - Central Power and Light Company, and the City of Austin. In-service dates for STP were August 1988 for Unit 1 and June 1989 for Unit 2. CPS' 28.0% ownership in the STP represents 700 megawatts of plant capacity. At January 31, 2005, CPS' investment in the STP utility plant was approximately \$1,700,000, net of accumulated depreciation. Effective November 17, 1997, the Participation Agreement among the owners of STP was amended and restated, and the STP Nuclear Operating Company (STP OPCO), a Texas non-profit non-member corporation created by the participants, assumed responsibility as the licensed operator of STP. The participants share costs in proportion to ownership interests, including all liabilities and expenses of STP OPCO.

CPS amortizes its share of nuclear fuel for the STP to fuel expense on a unit-of-production method. Under the Nuclear Waste Policy Act of 1982, the federal government assumed responsibility for the permanent disposal of spent nuclear fuel. CPS is charged a fee for disposal of spent nuclear fuel, which is based upon CPS' share of the STP generation that is available for sale to CPS customers. This charge is included in fuel expense monthly.

CPS has committed to acquire from AEP an additional 12% share of STP. This will increase ownership to 40.0% and will give CPS an additional 300 megawatts of plant capacity.

Nuclear Insurance

The Price-Anderson Act is a comprehensive statutory arrangement for providing limitations on liability and governmental indemnities with respect to nuclear accidents or events. The maximum amount that each licensee may be assessed following a nuclear incident at any insured facility is \$100,600, subject to adjustment for inflation, for the number of operating nuclear units and for each licensed reactor, payable at \$10,000 per year per reactor for each nuclear incident. CPS and each of the other participants of STP are subject to such assessments, which will be borne on the basis of their respective ownership interests in STP. For purposes of these assessments, STP has two licensed reactors. The participants have purchased the maximum limits of nuclear liability insurance, as required by law, and have executed indemnification agreements with the Nuclear Regulatory Commission (NRC), in accordance with the financial protection requirements of the Price-Anderson Act.

A Master Worker Nuclear Liability policy, with a maximum limit of \$300,000 for the nuclear industry as a whole, provides protection from nuclear-related claims.

NRC regulations require licensees of nuclear power plants to obtain on-site property damage insurance in a minimum amount of \$1,100,000. NRC regulations also require that the proceeds from this insurance be used first to ensure that the licensed reactor is in a safe and stable condition, so as to prevent any significant risk to the public health or safety, and then to complete any decontamination operations that may be ordered by the NRC. Any funds remaining would then be available for covering direct losses to property.

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(amounts are expressed in thousands)

10. CPS SOUTH TEXAS PROJECT (STP) (Continued)

Nuclear Insurance (Continued)

The owners of STP currently maintain \$2,800,000 of nuclear property insurance, which is above the legally required amount of \$1,100,000, but is less than the total amount available for such losses. The \$2,800,000 of nuclear property insurance consists of \$500,000 in primary property damage insurance and \$2,300,000 of excess property damage insurance, both subject to a retrospective assessment being paid by all members of Nuclear Electric Insurance Limited (NEIL). In the event that property losses as a result of an accident at the nuclear plant of any utility insured by NEIL exceed the accumulated funds available to NEIL, a retrospective assessment could occur. The maximum aggregate assessment under current policies for both primary and excess property damage insurance is \$25,500 during any one policy year.

Nuclear Decommissioning

CPS, together with the other owners of the STP, files with the NRC a certificate of financial assurance for the decommissioning of the nuclear power plant. The certificate assures that CPS will meet the minimum decommissioning funding requirements mandated by the NRC. The STP owners agreed in the financial assurance plan that their estimate of decommissioning costs would be reviewed and updated periodically. In 1995, the owners conducted a review of decommissioning costs. The results showed that CPS' share of decommissioning costs at approximately \$270,000 in 1994 dollars. In 1999, the owners conducted an additional review of decommissioning, and results estimated CPS' share of decommissioning costs are now approximately \$311,000 in 1998 dollars. In 2004, the owners conducted an additional review of decommissioning, and results showed that CPS' share of decommissioning costs are now approximately \$397,400 in 2004 dollars. Although there was an increase in decommissioning base costs from the 1998 study to the 2004 study, there was an offsetting decrease in applicable cost escalation assumptions. Therefore, CPS was able to decrease its minimum annual contribution requirement from \$15,900 in 2004 to \$6,900 in FY 2005. In fiscal year 2006, CPS expects to establish a funding level of approximately \$5,000.

In 1991, CPS started accumulating the decommissioning funds in an external trust, in accordance with the NRC's regulations. The Decommissioning Trust assets and related liabilities are included in CPS' financial statements as a component unit. At December 31, 2004, CPS has accumulated approximately \$222,400 of funds in the external trust. Based on the annual calculation of financial assurance required by the NRC, CPS' trust balance exceeded the calculated financial assurance amounts of \$77,300 at December 31, 2004.

Based upon the 1998 and 1994 decommissioning cost studies, the annual level funding into the trust of \$6,900 for 2005 was expensed by CPS.

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(amounts are expressed in thousands)

11. COMMITMENTS AND CONTINGENCIES

A. Primary Government (City)

Grants

The City has received significant financial assistance from federal and state agencies in the form of grants. The disbursement of funds received under these programs generally requires compliance with terms and conditions specified in the grant agreements and is subject to audit by the grantor agencies. Any disallowed claims resulting from such audits could become a liability of the General Fund or other applicable funds. However, in the opinion of management, liabilities resulting from disallowed claims, if any, will not have a materially adverse effect on the City's financial position at September 30, 2005. Grants awarded by federal, state, and other governmental agencies but not yet earned nor received in cash as of September 30, 2005, were \$114,546.

Capital Improvement Program

The City will be undertaking various capital improvements to its airport system during fiscal year 2006. The estimated cost of these improvements is \$149,276. Approximately \$11,508 of the total will be funded by federal grants.

Litigation

The City is involved in various lawsuits related to alleged personal and property damages, wrongful death, breach of contract, various claims from contractors for additional amounts under construction contracts, property tax assessments, environmental matters, class action and promotional practices, and discrimination cases. The Office of the City Attorney estimates the probable liability for these suits, including those mentioned below, will approximate \$8,995, which is included as a component of the reserve for claims liability in the amount of \$19,199. The estimated liability, including an estimate of incurred but not reported claims, is recorded in the Insurance Reserve Fund. The City makes significant estimates in determining the amounts of unsettled claims under its self-insurance program and believes that the self-insurance reserves recorded in the Self-Insurance Funds are adequate to cover losses for which the City may be liable. It is not determinable whether additional claims or revisions to estimates required for settlement on existing claims could have a material effect on the government-wide financial statements.

Charles and Tracy Pollock. Individually and as next friend of Sarah Jane Pollock, a minor child v. City of San Antonio. This is a nuisance case alleging that benzene gas emitted from the West Avenue Landfill caused chromosomal damage to a fetus during the period of gestation, resulting in Plaintiff's contracting acute lymphoblastic leukemia. Although the jury at trial entered a judgment of more than \$23,000 against the City, the trial court immediately reduced this by \$6,000. On appeal, the Fourth Court subsequently sided with the City and reduced the judgment further by eliminating \$10,000 in exemplary damages. The remaining issue is whether personal injuries are recoverable under the Plaintiff's theory of nuisance. The City believes they are not and that even if they are recoverable, damages are capped at \$250 under the Texas Tort Claims Act. The City is appealing to the Texas Supreme Court.

Matthew Jackson et. al. v. City of San Antonio. This is a Fair Labor Standards Act ("FLSA") lawsuit with 175 named plaintiffs who claim that they were required to report for duty 15 minutes prior to their shift and that they were not compensated for the time in violation of the FLSA. There are several other allegations based on the FLSA, as well. The lawsuit has been filed on behalf of all of the police officers similarly situated to the 175 plaintiffs. The Plaintiffs have a motion pending for class certification that could increase the size of the Plaintiff class to include all officers of the San Antonio Police Department, of which there are more than 2,000. Thus, the potential exists for more officers to join the lawsuit. The City expects to win the lawsuit, but the potential liability, if the case were lost, could be an amount well over \$1,000.

(amounts are expressed in thousands)

11. COMMITMENTS AND CONTINGENCIES (Continued)

A. Primary Government (City) (Continued)

Arbitrage

The City has issued certain tax-exempt obligations that are subject to Internal Revenue Service (IRS) arbitrage regulations. Non-compliance with these regulations, which pertain to the utilization and investment of proceeds, can result in penalties including the loss of the tax-exempt status of the applicable obligations retroactive to the date of original issuance. In addition, the IRS requires that interest income earned on proceeds in excess of the arbitrage rate on applicable obligations be rebated to the federal government. The City monitors its bond proceeds in relation to arbitrage regulations, and "arbitrage rebate" is estimated and recorded in the government-wide and proprietary financial statements when susceptible to accrual and in the governmental fund type when matured.

Leases

The City leases City-owned property to others consisting of buildings, real property, and parking spaces. Costs of specific leased components are not readily determinable. Total rental revenue on operating leases for fiscal year ended September 30, 2005, was \$17,945. As of September 30, 2005, the leases provide for the following future minimum rentals:

Leases Receivable				
	Governmental			Total
	Activities	Aviation	Parking	
Fiscal year ending September 30:				
2006	\$ 2,255	\$ 14,257	\$ 188	\$ 16,700
2007	1,422	2,503	73	3,998
2008	1,053	2,195	51	3,299
2009	697	1,625	36	2,358
2010	601	1,603	36	2,240
2011-2015	2,658	5,328	93	8,079
2016-2020	2,526	2,918		5,444
2021-2025	750	355		1,105
2026-2030	750	157		907
2031-2035	625			625
2036-2040	500			500
2041-2045	167			167
Future Minimum Lease Rentals	\$ 14,004	\$ 30,941	\$ 477	\$ 45,422

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(amounts are expressed in thousands)

11. COMMITMENTS AND CONTINGENCIES (Continued)

A. Primary Government (City) (Continued)

Landfill Postclosure Care Costs

In October 1993, the City Council approved closure of the Nelson Gardens Landfill, which immediately stopped accepting solid waste. Subsequent to landfill closure, federal and state laws required the City to incur certain postclosure care costs over a period of thirty years. As of September 30, 1994, the City estimated these costs for postclosure of the Nelson Gardens Landfill at \$3,800. The estimate was based on estimated costs for installation of a leachate and groundwater collection system, installation of a methane recovery system, geotechnical and environmental engineering services, and monitoring and maintaining the facility for a thirty-year period. In accordance with GASB Statement No. 18, *Accounting for Municipal Solid Waste Landfill Closure and Postclosure Care Cost*, the estimated postclosure cost of \$3,800 for the Nelson Gardens Landfill was recorded as a liability and expensed in the Environmental Services Fund in fiscal year 1994. This cost is an estimate and is subject to changes resulting from inflation/deflation, advances in technology, or changes in applicable laws or regulations.

Each fiscal year, the City performs an annual re-evaluation of the postclosure care costs associated with the Nelson Gardens Landfill. The annual re-evaluation conducted for the fiscal year ended September 30, 2005, resulted in an estimated postclosure care liability for the Nelson Gardens Landfill of \$1,030. This represents a decrease of \$21 from the prior fiscal year for expenditures incurred for geotechnical and environmental engineering services.

TCEQ Financial Assurance

The City is required under the provision of the Texas Administrative Code to provide financial assurance to the Texas Commission on Environmental Quality (TCEQ), formerly known as the Texas Natural Resource Conservation Commission (TNRCC), related to the closure of municipal solid waste operations including, but not limited to, storage, collection, handling, transportation, processing, and disposal of municipal solid waste. As such, financial assurance is required to ensure that funds are available, when needed, to meet costs associated with the closure of the City's North East Transfer Station. Additionally, financial assurance is required to demonstrate financial responsibility for underground storage petroleum facilities. As of September 30, 2001, the permit for the North East Transfer Station has been transferred from the City, and the new permittee has provided adequate financial assurance for this facility. Based on the number of underground petroleum storage tanks, the City is required to provide \$1,000 of financial assurance related to the underground storage facilities.

Brooks City-Base – Electric and Gas Utilities

The Brooks City-Base Project is a collaborative effort between the U.S. Air Force (the "Air Force") and the City designed to retain the Air Force missions and jobs at Brooks Air Force Base, improve mission effectiveness, assist in reducing operating costs, and promote and enhance economic development at Brooks. On July 22, 2002, the land and improvements were transferred to the Brooks Development Authority (BDA) for the purpose of creating the Brooks Technology & Business Park, a facility that will foster the development of key targeted industries. The Air Force is currently the Park's anchor tenant and is leasing back facilities to perform its missions.

As part of the conveyance, the electric and gas utilities were transferred to City Public Service (CPS), the City's utility. The electric and gas utility systems' infrastructure at Brooks are deficient and require extensive upgrades and improvements. Pursuant to the transfer, the Air Force, BDA, and CPS have committed to make certain improvements and upgrades to the electric and gas utility over a 20-year period. Funding for these improvements include \$3,400 from the City and \$6,300 from BDA and CPS each, respectively, for a total of \$16,000.

(amounts are expressed in thousands)

11. COMMITMENTS AND CONTINGENCIES (Continued)

A. Primary Government (City) (Continued)

Brooks City-Base – Electric and Gas Utilities (Continued)

With respect to BDA's obligation of \$6,300, the City has agreed, under certain circumstances and if necessary, to assist BDA in funding its obligation. The City has agreed to contribute to BDA on an annual basis an amount equivalent to the incremental increase in the City's payment from CPS derived from Brooks. The City, as the owner of CPS, receives 14.0% of CPS' gross revenues, and this amount represents additional resources available to the City as a result of its increased payment from CPS derived at Brooks. Over the 20-year period, the City's annual payments will not exceed \$3,400. In the event BDA has exhausted all of its available resources and has been unable to fulfill its obligation of \$6,300 by the end of the 20-year term, the City has agreed in good faith to utilize all of its funding options to enable BDA to satisfy its obligation.

B. City Public Service (CPS)

Joint Operations Agreement

A 1997 Joint Operations Agreement (JOA) resulted from the litigation settlement with Texas Genco, L.P., formerly known as Reliant Energy, Inc., and Houston Lighting & Power, over its management of STP during the construction and early operating periods. The JOA is an arrangement to jointly dispatch CPS' and Texas Genco, L.P.'s generating plants to take advantage of the most efficient plants and favorable fuel prices of each utility. Until June 2002, CPS received, in monthly cash payments, 90.0% of the savings realized from the jointly operated systems. As of June 2002, when Texas Genco, L.P. met the JOA \$200,000 cumulative savings obligation, monthly cash payments were reduced to 50% of the savings realized from the jointly operated systems. As of January 31, 2005, CPS' total cumulative payments from savings realized was \$265,500.

Litigation

Additionally, in the normal course of business, CPS is involved in other legal proceedings related to alleged personal and property damages, breach of contract, condemnation appeals, and discrimination cases. Also, CPS power generation activities and other utility operations are subject to extensive state and federal environmental regulation. In the opinion of management of CPS, the outcome of such proceedings will not have a material adverse effect on the financial position or results of operations of CPS.

Other

Purchase and construction commitments amounted to approximately \$893,000 at January 31, 2005. This amount includes approximately \$24,400 that is expected to be paid for natural gas purchases to be made under various contracts currently in effect through June 2007; the actual amount to be paid will depend upon CPS' actual requirements during the contract period and the price of gas. Also included is \$54,800 for coal purchases through December 2006, \$238,400 for coal transportation through December 2014, and \$3,000 for treated cooling water through December 2005, based upon the minimum firm commitment under these contracts.

CPS has also committed to purchase \$229,700 in wind power. Additional purchase commitments at January 31, 2005, which are related to STP, include approximately \$45,500 for raw uranium, associated fabrication, and conversion services. This amount represents services that will be needed for refueling through the year 2028.

The PLC promulgated new rules in 1996 designed to comply with legislative changes affecting the utility industry. The Transmission Pricing and Access Rule (Rule) mandates that electric utilities charge customers for wholesale open transmission access according to a formula based on the amount of load served by each utility. CPS' cost for calendar year 2004 was approximately \$15,800. The estimated cost for calendar year 2005 is approximately \$15,100.

(amounts are expressed in thousands)

11. COMMITMENTS AND CONTINGENCIES (Continued)**Other (Continued)****B. City Public Service (CPS) (Continued)**

As part of the Request for Proposal process for the J.K. Spruce Unit 2 Power Plant, CPS has committed to compensate the unsuccessful J.K. Spruce 2 Design-Build Offeror up to \$1,000, which is payable contingent on their meeting specific criteria.

C. San Antonio Water System (SAWS)**Litigation**

SAWS is the subject of various claims and litigation that have risen in the ordinary course of its operations. Management, in consultation with legal counsel, is of the opinion that SAWS' liabilities in these cases, if decided adversely to SAWS, will not be material.

Other

SAWS is committed under various contracts for completion of construction or acquisition of utility plants totaling approximately \$182,440 as of December 31, 2004. Funding of this amount will come from available revenues of SAWS, contributions from developers, and restricted assets.

12. RISK FINANCING**A. Primary Government (City)****Property and Casualty Liability**

At September 30, 2005, the City has excess insurance coverage through State National Insurance Company for liability. The blanket policy provides general and auto liability along with police professional errors and omissions and EMS Medical Malpractice, and Civil Rights and Employee Benefits Liability Coverage. Allianz Insurance Company provides property coverage on the City's building and contents inventory. The City utilizes a third-party administrator for the handling of administration, investigation, and adjustment of liability claims.

Obligations for claims under these programs are accrued in the City's Self-Insurance Reserve Internal Service Fund based on the City's estimates of the aggregate liability for claims made and claims incurred but not reported, and Departments are assessed premiums to cover expenditures. There were no significant reductions in insurance coverage. Claims settlements did not exceed insurance coverage for each of the past three years.

Employee Health Benefits

The City provides its current employees with a comprehensive employee benefit program including coverage for medical, dental, and life insurance, vision, dependent care reimbursement accounts, and additional life insurance for its employees and their dependents. The City's self-insured medical programs are provided to all City employees. Obligations for benefits are accrued in the City's Self-Insurance Employee Benefits Insurance Internal Service Fund based upon the City's estimates of the aggregate liability for unpaid benefits.

(amounts are expressed in thousands)

12. RISK FINANCING (Continued)**A. Primary Government (City) (Continued)****Workers' Compensation**

The City self-insures for Workers' Compensation. The City is a member of the Texas Municipal League (TML) Workers' Compensation Joint Insurance Fund, an unincorporated association of political subdivisions of the State of Texas. The TML Workers' Compensation Joint Insurance Fund is not intended to operate as an insurance company, but rather is intended to be a contracting mechanism, which the City as a member utilizes to administer self-insurance workers' compensation benefits to its employees for claims that occurred prior to September 30, 1986. The City also utilizes third-party administrators for the handling of administration, investigation, and adjustment of workers' compensation claims that occurred after October 1, 1986. All loss contingencies, including claims incurred but not reported, if any, are recorded in the City's Self-Insurance Workers' Compensation Internal Service Fund and City departments are assessed premiums to cover expenditures. As of September 30, 2005, the City has excess workers' compensation coverage through the State National Insurance Company. Claims settlements did not exceed insurance coverage for each of the past three years.

Unemployment Compensation Program

The Unemployment Compensation Program of the Self-Insurance Internal Service Fund provides a central account for payment of unemployment compensation claims. As of the fiscal year-end, claims were being administered internally by the City and are paid to the Texas Workforce Commission on a reimbursement basis. All costs incurred are recorded on a claim paid basis.

Extended Sick Leave Program

The Extended Sick Leave Program of the Self-Insurance Internal Service Fund is used to pay benefits associated with the City's employee long-term disability plan. Benefits are administered by the City. Actual costs are incurred when extended leave is taken.

Employee Wellness Program

The Self-Insurance Employee Wellness Program Internal Service Fund is used to account for revenues and operating expenses of the City Occupational Health Clinic operated by the San Antonio Metropolitan Health District. The clinic's operation is supported by transfers from the Workers' Compensation Fund and the Employee Health Benefits Fund as expenses are incurred. In fiscal year 1999, the Employee Assistance Program was established to offer City employees short-term mental health, marital, and financial counseling, as well as substance abuse intake and assessment. The Program was funded by a transfer from the Workers' Compensation Fund.

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(amounts are expressed in thousands)

12. RISK FINANCING (Continued)**A. Primary Government (City) (Continued)****Claims Liability**

The liability for the Employees' Benefits Program is based on the estimated aggregate amount outstanding at the statement of net assets date for unpaid benefits. Liabilities for the Insurance Reserve and Workers' Compensation Programs are reported when it is probable that a loss has occurred as of the statement of net assets date, and the amount of the loss can be reasonably estimated. These liabilities include allocable loss adjustment expenses, specific incremental claim adjustment expenses such as the cost of outside legal counsel, and a provision for claims that have been incurred but not reported (IBNR). Unallocated claim adjustment expenses have not been included in the calculation of the outstanding claims liability as management of the City feels it would not be practical or cost beneficial. In addition, based on the difficulty in determining a basis for estimating potential recoveries and the immateriality of prior amounts, no provision for subrogation or salvage has been included in the calculation of the claims liability. The claims liability reported in the accompanying financial statements for the Insurance Reserve Program is based on a 3.0% discounted rate.

The following is a summary of changes in claims liability for the City's Insurance Reserve, Employee Benefits, and Workers' Compensation Programs for the year ended September 30, 2005.

Fund	Schedule of Changes In Claims Liability				
	Liability Balance October 1,	Change in Estimates	Claims & Adjustments	Claims Payments	Liability Balance September 30, ¹
<u>Insurance Reserve</u>					
Fiscal Year 2004	\$ 16,179	\$ 1,092	\$ 3,370	\$ (3,370)	\$ 17,271
Fiscal Year 2005	17,271	1,928	4,638	(4,638)	19,199
<u>Employee Benefits</u>					
Fiscal Year 2004	\$ 8,548	\$ —	\$ 48,266	\$ (48,266)	\$ 8,548
Fiscal Year 2005	8,548	—	66,489	(66,489)	8,548
<u>Workers' Compensation¹</u>					
Fiscal Year 2004	\$ 23,205	\$ —	\$ 9,635	\$ (9,635)	\$ 23,205
Fiscal Year 2005	23,205	(1,326)	10,297	(10,297)	21,879

¹The Workers' Compensation Liability Balance of \$21,879 is comprised of \$19,553 recorded in the Workers' Compensation Fund and the remaining liability of \$2,326 is recorded in Proprietary Funds.

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(amounts are expressed in thousands)

12. RISK FINANCING (Continued)**B. City Public Service (CPS)**

CPS is exposed to various risks of loss including those related to torts, theft or destruction of assets, errors and omissions, and natural disasters. CPS purchases commercial liability and property insurance coverages to provide protection in event of large/catastrophic claims. CPS performs actuarial studies periodically to determine its insurance retentions. An actuarial study was last performed in 2004.

In addition, CPS is exposed to risks of loss due to death of, and injuries to, or illness of, its employees. CPS makes payments to external trusts to cover the claims under the related plans. At January 31, 2005, CPS accumulated approximately \$172,800 in these external trusts. The trust accounts and related claims liabilities are included in CPS' financial statements. CPS has recorded \$30,400 of expense related to these plans for the year ended January 31, 2005.

Based upon the guidance of GASB Statement No. 10, *Accounting and Financial Reporting for Risk Financing and Related Insurance Issues*, the following information is provided regarding the changes in the insurance reserves for property and employee and public liability claims for the years ended January 31:

Fund	City Public Service Schedule of Changes In Claims Liability			
	Liability Balance February 1,	Claims & Adjustments	Claims Payments	Liability Balance January 31,
<u>Property Insurance</u>				
Fiscal Year 2004	\$ 5,553	\$ 377	\$ (95)	\$ 5,835
Fiscal Year 2005	5,835	1,010	—	6,845
<u>Employee & Public Liability Claims</u>				
Fiscal Year 2004	\$ 6,866	\$ 1,371	\$ (1,000)	\$ 7,237
Fiscal Year 2005	7,237	(871)	(331)	6,035
<u>Employee Health & Welfare Claims</u>				
Fiscal Year 2004	\$ 4,172	\$ 35,939	\$ (35,415)	\$ 4,696
Fiscal Year 2005	4,696	32,888	(32,325)	5,259

The employee health and welfare plan assets are segregated from CPS' assets. They are separately managed by a committee whose members are appointed by the CPS General Manager and CEO. These plans have separate financial statements for calendar year 2004. These separately audited financial statements are available upon request from CPS.

(amounts are expressed in thousands)

12. RISK FINANCING (Continued)**C. San Antonio Water System (SAWS)****Risk Management**

SAWS is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters.

SAWS is self-administered and self-insured for the first \$500 of each worker's compensation, general liability, automobile liability, public official's liability and \$250 for pollution legal liability claim whereby any claim exceeding the self-insured retention limit would be covered through SAWS' comprehensive commercial insurance program. For the year ended December 31, 2004, there were no reductions in insurance coverage from the previous year and there were no claims that exceeded the self-insured retention limit. Settled claims have not exceeded the insurance coverage in any of the past three fiscal years.

SAWS had recorded a liability in the amount of \$2,477 as of December 31, 2004, which is reported as a current liability. The claims liability, including incurred but not reported claims, is based on the estimated ultimate cost of settling the claims. The claims liability includes medical and rehabilitation costs, which are considered incremental claim adjustment expenses. Changes in the liability amount for the last two fiscal years were:

San Antonio Water System Schedule of Changes In Claims Liability				
Year Ended	Balance at Beginning of Fiscal Year Liability	Claims & Adjustments	Claims Payments	Balance at End of Fiscal Year Liability
Dec. 31, 2003	\$ 1,184	\$ 3,029	\$ (1,896)	\$ 2,317
Dec. 31, 2004	\$ 2,317	\$ 1,675	\$ (1,515)	\$ 2,477

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(amounts are expressed in thousands)

13. INTERFUND TRANSFERS

The following is a summary of interfund transfers for the City for the year ended September 30, 2005:

Summary Table of Interfund Transfers Year Ended September 30, 2005		
	Transfers From Other Funds	Transfers To Other Funds
General Fund:	\$	102 \$
Airport System		760 499
Parking Facilities		766 3,705
Internal Service Funds		11,184 81,752
Nonmajor Governmental Funds		1,310
Nonmajor Enterprise Fund		14,122 85,956
Total General Fund		
Debt Service Funds:		
Nonmajor Governmental Funds		16,423
Total Debt Service Funds		16,423
Airport System Fund:		
General Fund		102
Internal Service Funds		151
Nonmajor Governmental Funds		362
Total Airport System Fund		615
Parking Facilities Fund:		
General Fund	499	760
Internal Service Funds		39
Nonmajor Governmental Funds		228
Total Parking Facilities Fund	499	1,027
Internal Service Funds:		
General Fund	3,705	766
Airport System	151	
Parking Facilities	39	
Internal Service Funds	1,399	1,399
Nonmajor Governmental Funds	380	351
Nonmajor Enterprise Fund	212	430
Total Internal Service Funds	5,886	2,946
Nonmajor Governmental Funds:		
General Fund	81,752	11,184
Debt Service		16,423
Airport System	362	
Parking Facilities	228	
Internal Service Funds	351	380
Nonmajor Governmental Funds	46,583	46,583
Nonmajor Enterprise Fund		85
Total Nonmajor Governmental Funds	129,276	74,655
Nonmajor Enterprise Fund:		
General Fund		1,310
Internal Service Funds	430	212
Nonmajor Governmental Funds	85	
Total Nonmajor Enterprise Funds	515	1,522
Total	\$ 166,721	\$ 166,721

(amounts are expressed in thousands)

13. INTERFUND TRANSFERS (Continued)

Transfers are made to use unrestricted revenues collected in the General Fund to finance various programs accounted for in other funds. These transfers are in the form of operating subsidies, grant matches, and funding for capital projects. In addition, transfers are routinely made from other funds to fund debt service payments and for other restricted purposes. All transfers are in accordance with budgetary authorizations.

Other significant transfers by the General Fund include \$615 set aside for the purchase of additional ladder trucks from fiscal year 2006 through fiscal year 2009. This is the third year that funds have been set aside for that purpose as the Master Plan recommended in fiscal year 2001 that \$615 in funds be set aside each year through fiscal year 2005.

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(amounts are expressed in thousands)

14. RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

A. Explanation of certain differences between the governmental fund balance sheet and the government-wide statement of net assets

The governmental fund balance sheet includes a reconciliation between fund balance - total governmental funds and net assets-governmental activities as reported in the Government-wide Statement of Net Assets.

One element of this reconciliation states, "Some of the City's revenues will be collected after year-end but are not available soon enough to pay for the current period's expenditures and, therefore, are not reported in the governmental funds." The detail of the \$23,958 is as follows:

Revenues previously reported as deferred in the fund financial statements	\$ 33,528
Receivable applicable to governmental activities, which are not available in the current period	565
Deferred revenues previously reported as income in the fund financial statements	<u>(10,135)</u>
Revenues collected after year end but are not available soon enough to pay for the current period's expenditures and therefore are not recognized in governmental funds	<u>\$ 23,958</u>

Another element of this reconciliation states, "Long-term liabilities, including bonds payable, are not due and payable in the current period and, therefore, are not reported in the governmental funds." The detail for the decrease related to capital leases is as follows:

Total capital leases reported on the Government-wide Statement of Net Assets	\$ 7,232
Less: Short-term available portion reported in fund financial statements	<u>(1,153)</u>
Net adjustment to decrease fund balance-total governmental funds to arrive at new assets-governmental activities for capital leases	<u>\$ 6,079</u>

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(amounts are expressed in thousands)

14. RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS (Cont'd)

B. Explanation of Certain Differences Between the Governmental Fund Statement of Revenues, Expenditures, and Changes in Fund Balance and the Government-wide Statement of Activities

The governmental fund Statement of Revenues, Expenditures, and Changes in Fund Balances includes a reconciliation between net changes in fund balances - total governmental funds and changes in net assets of governmental activities as reported in the Government-wide Statement of Activities.

The details of the increase of bond premiums and deferred charges are as follows:

Amortization of bond premiums on long-term debt-Debt Service Fund, previously expensed in the fund financial statements	\$ 1,027
Amortization of bond premiums and bond issues costs on long-term debt - General Obligation Bonds previously expensed in the fund financial statements	18,725
Less: premiums on bonds and certificates not previously recorded in the fund financial statements	(5,031)
Total amortization of bond premiums and deferred charges (net)	\$ 14,721

Another element of this reconciliation states, "Some expenses reported in the Statement of Activities are not reported as expenditures in governmental funds." The details of the (\$9,990) are as follows:

Compensated Absences	\$ (6,557)
Interest Expense	(6,505)
Principal Paid on Leases	3,792
Arbitrage Rebate Expense	(720)
Net adjustment to decrease net changes in fund balances - total governmental funds to arrive at changes in net assets of governmental activities.	\$ (9,990)

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(amounts are expressed in thousands)

15. DEFICITS IN FUND BALANCES / NET ASSETS

Special Revenue Funds

The Alamodome Fund had a deficit fund balance of \$3,199 as of September 30, 2005. This deficit is attributed to events programmed but not realized, due in part to the downturn of certain entertainment industries and local venue competition. Additionally, individual spending per event was expected to increase due to an anticipated economic upswing.

The Public Health Support Revenue Fund had deficit fund balance of \$131 as of September 30, 2005. The deficit is attributed to increased operating costs associated with the expansion of the Animal Care Project. Higher commodity expenditures were the result of an active influenza season and increased vaccine cost.

As of September 30, 2005, deficit fund balance at year-end is reported in the Categorical Grant In-Aid, and Community Development Program in the amounts of \$3,934 and \$251, respectively. During the next fiscal year, individual projects within the Categorical Grant-In Aid Fund which have a deficit fund balance will be comprehensively researched and analyzed to determine whether insufficient funding exists or accounting adjustments to projects are required to be made. Once this process is completed, a corrective action plan to address the deficit fund balance will be developed and implemented in Fiscal Year 2006. The deficit for the Community Development Program Fund is attributable to project budgets that require adjustment in order to address these deficits.

The Golf Course Fund had a deficit fund balance of \$974 as of September 30, 2005. The deficit is attributable to a decline in revenues in recent years due to increased competition by the private sector and extreme weather patterns. In addition, increased labor, fuel, and equipment maintenance costs have contributed to the deficit.

Internal Service Funds

As of September 30, 2005, a deficit of \$20,689 in net assets is reported in the Employee Benefits Program. This deficit decreased by \$11,063 from the prior fiscal year. To address specific issues related to the increasing costs of health benefits, the City has sought the services of an outside consultant in 2006 to perform a comprehensive review of the Employee Benefits Programs. Establishing health care medical management programs focused on providing managed care for employees having chronic, high-risk ailments involving high costs such as back pain, high-risk maternity, heart disease, and depression are some of the areas on which the consultant will be focusing. Programs such as these will be carefully studied as means of providing long-term solutions to address rising health care costs and increasing fund balance deficits.

Within the Internal Service Funds, the Workers' Compensation Program also reported deficit net assets of \$4,245, at September 30, 2005, which was reduced by \$2,345 from the prior fiscal year. The City will fund the deficit through assessments charged to various City funds in future years.

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(amounts are expressed in thousands)

16. OTHER DISCLOSURES

Donor Restricted Endowment

The City of San Antonio has four permanent funds: the San Jose Burial Park Permanent Fund, the Carver Cultural Center Endowment Fund, the San Antonio Housing Trust Fund, and the William C. Morris Endowment Fund. The City is only allowed to spend interest proceeds generated from the principal amount for each of these funds. The net assets from these endowment funds are classified as restricted net assets and are reported in the government-wide financial statements. The principal is required to be retained in perpetuity while the interest is available to cover specific expenditures.

The San Jose Burial Park Permanent Fund generated \$54 in interest to be expended for specified purposes. Chapter 713 of the Texas Health and Safety Code governs what expenditures the City may incur when spending the interest income. Per Chapter 713, the revenue can be spent for the maintenance and care of the graves, lots, and burial places, and to beautify the entire cemetery. The principal amount of this fund is increased each year by sales of lots from the San Jose Cemetery.

The Carver's Endowment Fund generated \$8 in interest. These earnings can be used for the Carver Community Cultural Center's operating program, or reinvestment expenses (as detailed in the grant agreement). This fund is managed in accordance with the Uniform Management of Institutional Funds Act, which is codified as Section 163.001 in the Texas Property Code. The principal portion of the fund came from a one-time grant from the National Endowment for the Arts.

The San Antonio Housing Trust Fund generated \$314 in interest. These earnings may be disbursed to projects with particular emphasis on housing programs as grants or secured loans. All distributions or disbursements of this trust shall be made for the primary purpose of providing additional and continuing housing opportunities for low and moderate income families. This trust shall at all times be governed, construed, regulated, and administered in all respects under the laws of the State of Texas.

The William C. Morris Endowment Fund generated \$5 in interest. These earnings are used on an annual basis to enhance the City's Library's Educational Programming and Services for Children. Any net income or net appreciation of the funds not used shall be accumulated and added to the principal of the funds. The earnings of the funds will be expended in accordance with the spending policy of the Library's Board of Directors or Trustees.

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(amounts are expressed in thousands)

17. SUBSEQUENT EVENTS

Primary Government (City)

On December 2, 2004, the City issued \$33,090 of "City of San Antonio, Texas General Improvement Forward Refunding Bonds, Series 2006," (the "2006 Bonds"). The 2006 Bonds were delivered on May 9, 2006. The 2006 Bonds have maturities from 2009 to 2016, with interest rates ranging from 5.25% to 5.50%.

Fire Collective Bargaining Agreements

The City's collective bargaining agreement with the International Association of Fire Fighters Local 624 ("Local 624") approved on May 23, 2003 had a term of June 3, 2002 through September 30, 2005. The contract contains an evergreen clause effective through September 30, 2015. Negotiations for a new agreement with the Local 624 have been initiated, however, to date, no agreement has been reached.

Response to Hurricanes Katrina and Rita

On August 29, 2005, Hurricane Katrina landed on the coasts of Louisiana, Mississippi and Alabama. The catastrophic destruction caused by the hurricane led to an unprecedented amount of evacuees seeking shelter in the City of San Antonio. Additionally, on September 24, 2005, Hurricane Rita caused extensive damage to the coastal regions of Texas and Louisiana. The City combined forces with Bexar County, private companies, and state, federal, and non-profit agencies to coordinate the needed relief efforts in order to assist the evacuation efforts for Hurricanes Katrina and Rita. The City as of April 2006, has incurred approximately \$35,031 in shelter and interim housing expenses in support of the relief efforts consisting of temporary housing, equipment, food, medical supplies, facilities, and City emergency and civilian personnel. Additionally, the City has been reimbursed \$27,134 from the Federal Emergency Management Agency (FEMA). The remaining eligible expenses of \$7,897 have been submitted to FEMA for reimbursement. FEMA will accordingly reimburse the additional costs.

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(amounts are expressed in thousands)



***City of San Antonio
Texas***

***Required Supplementary Information Other Than MD&A
(Unaudited)***

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***City of San Antonio
Texas***

Budgetary Comparison Schedule - General Fund

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CITY OF SAN ANTONIO, TEXAS

GENERAL FUND
BUDGETARY COMPARISON SCHEDULE
YEAR ENDED SEPTEMBER 30, 2005

	2005			VARIANCE WITH FINAL BUDGET POSITIVE (NEGATIVE)
	BUDGETED AMOUNTS		ACTUAL	
	ORIGINAL	FINAL		
<u>Resources (Inflows):</u>				
Taxes	\$ 350,282,729	\$ 350,282,729	\$ 367,030,243	\$ 16,747,514
Licenses and Permits	17,542,550	17,542,550	20,715,743	3,173,193
Intergovernmental	2,795,306	2,795,306	3,055,128	259,822
Revenues from Utilities	196,784,803	196,784,803	221,774,673	24,989,870
Charges for Services	29,101,948	29,101,948	33,622,089	4,520,141
Fines and Forfeits	12,315,804	12,315,804	12,025,344	(290,460)
Miscellaneous	11,668,023	11,668,023	14,286,093	2,618,070
Transfers from Other Funds	14,673,148	14,778,703	14,121,847	(656,856)
Amounts Available for Appropriation	635,164,311	635,269,866	686,631,160	51,361,294
<u>Charges to Appropriations (Outflows):</u>				
General Government	79,512,765	87,405,500	66,746,538	20,658,962
Public Safety	400,696,219	405,154,154	404,491,342	662,812
Public Works	10,698,288	10,698,288	10,477,765	220,523
Health Services	13,947,697	14,245,069	14,378,887	(133,818)
Sanitation	2,886,374	2,886,374	2,582,840	303,534
Welfare	20,837,267	22,018,578	21,578,358	440,220
Culture and Recreation	66,031,937	66,726,827	63,478,741	3,248,086
Economic Development and Opportunity	4,054,036	4,525,265	4,552,704	(27,439)
Transfers to Other Funds	75,209,927	87,057,100	86,649,587	407,513
Total Charges to Appropriations	673,874,510	700,717,155	674,936,762	25,780,393
Excess (Deficiency) of Resources Over (Under)				
Charges to Appropriations	(38,710,199)	(65,447,289)	11,694,398	77,141,687
Fund Balance Allocation	38,710,199	65,447,289	(11,694,398)	(77,141,687)
<u>Excess (Deficiency) of Resources Over (Under)</u>				
<u>Charges to Appropriations</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

Explanation of Differences between Budgetary Inflows and Outflows and GAAP Revenues and Expenditures

Sources/Inflows of Resources:

Actual amounts (budgetary basis) "available for appropriation" from the budgetary comparison schedule \$ 686,631,160

Differences - budget to GAAP:

Transfers from other funds are inflows of budgetary resources but are not revenues for financial reporting purposes (14,121,847)

Total revenues as reported on the statement of revenues, expenditures, and changes in fund balances - governmental funds \$ 672,509,313

Uses/Outflows of Resources:

Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule. \$ 674,936,762

Differences - budget to GAAP:

Encumbrances for supplies and equipment ordered but not received is reported in the year the order is placed for budgetary purposes, but in the year the supplies are received for financial reporting purposes. (7,514,793)

Transfers to other funds are outflows of budgetary resources but are not expenditures for financial reporting purposes. (86,649,587)

Total expenditures as reported on the statement of revenues, expenditures, and changes in fund balances - governmental funds \$ 580,772,382

General Fund Budgetary Information

The City Charter establishes requirements for the adoption of budgets and budgetary control. Under provisions of the Charter, expenditures of each City function and activity within individual funds cannot legally exceed the final budget approved by the City Council. Amendments to line items within a departmental budget may be initiated by Department Directors.

The City prepares an annual budget for the General Fund on a modified-accrual basis, which is consistent with generally accepted accounting principles. The annual budgetary data reported for the General Fund represents the original appropriation ordinance and amendments thereto as adopted by the City Council, adjusted for encumbrances outstanding at the beginning of the fiscal year. All annual appropriations lapse at fiscal year-end.

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***City of San Antonio
Texas***

Pension Schedules

REQUIRED SUPPLEMENTARY INFORMATION - (UNAUDITED)
SCHEDULES OF FUNDING PROGRESS
LAST THREE FISCAL YEARS

FIRE AND POLICE PENSION PLAN--CITY OF SAN ANTONIO

ACTUARIAL VALUATION DATE	ACTUARIAL VALUE OF ASSETS	ENTRY AGE ACTUARIAL ACCRUED LIABILITY (AAL)	UNFUNDED ACTUARIAL ACCRUED LIABILITY (UAAL)	FUNDED RATIO	COVERED PAYROLL	UAAL AS A PERCENTAGE OF COVERED PAYROLL
10-01-04	\$ 1,540,286	\$ 1,838,371	\$ 298,085	84%	\$ 204,516	146%
10-01-03	1,429,378	1,718,262	288,884	83%	191,647	151%
10-01-02	1,341,274	1,630,434	289,160	82%	183,686	157%

TEXAS MUNICIPAL RETIREMENT SYSTEM--CITY OF SAN ANTONIO

ACTUARIAL VALUATION DATE	ACTUARIAL VALUE OF ASSETS	UNIT CREDIT ACTUARIAL ACCRUED LIABILITY (AAL)	UNFUNDED ACTUARIAL ACCRUED LIABILITY (UAAL)	FUNDED RATIO	COVERED PAYROLL (1)	UAAL AS A PERCENTAGE OF COVERED PAYROLL
12-31-04	\$ 464,345	\$ 621,034	\$ 156,689	75%	\$ 204,088	77%
12-31-03	451,071	602,927	151,856	75%	192,896	79%
12-31-02	436,046	566,203	130,157	77%	197,678	66%

CITY PUBLIC SERVICE ALL EMPLOYEE PLAN

ACTUARIAL VALUATION DATE	ACTUARIAL VALUE OF ASSETS	UNIT CREDIT ACTUARIAL ACCRUED LIABILITY (AAL)	UNFUNDED ACTUARIAL ACCRUED LIABILITY (UAAL)	FUNDED RATIO	COVERED PAYROLL	UAAL AS A PERCENTAGE OF COVERED PAYROLL
01-01-04	\$ 839,800	\$ 795,100	\$ (44,700)	106%	\$ 189,900	(24)%
01-01-03	783,000	748,700	(34,300)	105%	186,700	(18)%
01-01-02	758,200	691,800	(66,400)	110%	180,300	(37)%

NOTES: (1) Abstracted from City payroll records.

(amounts are expressed in thousands)

(unaudited - see accompanying accountants' report)

REQUIRED SUPPLEMENTARY INFORMATION - (UNAUDITED)
SCHEDULES OF FUNDING PROGRESS
LAST THREE FISCAL YEARS

SAN ANTONIO WATER SYSTEM - TMRS

ACTUARIAL VALUATION DATE	ACTUARIAL VALUE OF ASSETS	UNIT CREDIT ACTUARIAL ACCRUED LIABILITY (AAL)	UNFUNDED ACTUARIAL ACCRUED LIABILITY (UAAL)	FUNDED RATIO	COVERED PAYROLL	UAAL AS A PERCENTAGE OF COVERED PAYROLL
12-31-04	(2) \$	\$	\$		\$	
12-31-03	48,964	61,425	12,461	80%	57,596	22%
12-31-02	46,492	57,635	11,143	81%	51,889	21%
12-31-01	44,613	55,201	10,588	81%	51,958	20%

SAN ANTONIO WATER SYSTEM - PMLIC

ACTUARIAL VALUATION DATE	ACTUARIAL VALUE OF ASSETS	ENTRY AGE ACTUARIAL ACCRUED LIABILITY (AAL)	UNFUNDED ACTUARIAL ACCRUED LIABILITY (UAAL)	FUNDED RATIO	COVERED PAYROLL	UAAL AS A PERCENTAGE OF COVERED PAYROLL
01-01-04	\$	\$	\$		\$	
01-01-03	47,249	57,241	9,992	83%	56,932	18%
01-01-02	42,827	52,602	9,775	81%	55,364	18%
	39,270	45,947	6,677	85%	51,303	13%

(2) Balances for 12/31/04 not available

(amounts are expressed in thousands)

(unaudited - see accompanying accountants' report)

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APPENDIX D

DTC'S BOOK ENTRY-ONLY SYSTEM

DTC, the world's largest depository, is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 2.2 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments from over 85 countries that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly owned subsidiary of the Depository Trust & Clearing Corporation ("DTCC"). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Fixed Income Clearing Corporation, and Emerging Markets Clearing Corporation (NSCC, FICC, and EMCC, also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has Standard & Poor's highest rating: "AAA". The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com and www.dtc.org.

Purchases of Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Bonds on DTC's records. The ownership interest of each actual purchaser of each Bond ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in Bonds, except in the event that use of the book-entry system for the Bonds is discontinued.

To facilitate subsequent transfers, all Bonds deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

Redemption notices will be sent to DTC. If less than all of the Bonds within an issue are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the Bonds unless authorized by a Direct Participant in accordance with DTC's procedures. Under its usual procedures, DTC mails an "Omnibus Proxy" to the City as soon as possible after the record date. The Omnibus Proxy assigns Cede &

Co.'s consenting or voting rights to those Direct Participants to whose accounts Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Redemption proceeds, principal, and interest payments on the Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the City or the Paying Agent/Registrar, on the payment date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC, the Paying Agent/Registrar, or the City, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, principal, and interest payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the City or the Paying Agent/Registrar; disbursement of such payments to Direct Participants will be the responsibility of DTC; and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as depository with respect to the Bonds at any time by giving reasonable notice to the City or the Paying Agent/Registrar. Under such circumstances, in the event that a successor depository is not obtained, Bonds are required to be printed and delivered.

Under the Ordinance, the Registered Owners may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Bond certificates will be printed and delivered.

APPENDIX E

FORM OF BOND COUNSEL OPINION

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LAW OFFICES
McCALL, PARKHURST & HORTON L.L.P.

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DALLAS, TEXAS 75201-6587
TELEPHONE: 214 754-9200
FACSIMILE: 214 754-9250

700 N. ST. MARY'S STREET
1525 ONE RIVERWALK PLACE
SAN ANTONIO, TEXAS 78205-3503
TELEPHONE: 210 225-2800
FACSIMILE: 210 225-2984

600 CONGRESS AVENUE
1250 ONE AMERICAN CENTER
AUSTIN, TEXAS 78701-3248
TELEPHONE: 512 478-3805
FACSIMILE: 512 472-0871

Proposed Form of Opinion of Bond Counsel

*An opinion in substantially the following form will be delivered by
McCall, Parkhurst & Horton L.L.P., Bond Counsel,
upon the delivery of the Series 2006 Bonds, assuming no material changes in facts or law.*

December __, 2006

**CITY OF SAN ANTONIO, TEXAS
AIRPORT SYSTEM REVENUE REFUNDING BONDS, SERIES 2006
DATED NOVEMBER 1, 2006
IN THE AGGREGATE PRINCIPAL AMOUNT OF \$17,850,000**

AS BOND COUNSEL FOR THE CITY OF SAN ANTONIO, TEXAS (the "City"), the issuer of the Bonds described above (the "Series 2006 Bonds"), we have examined into the legality and validity of the Series 2006 Bonds, which bear interest from November 1, 2006, until maturity, at the rates stated in the text of the Series 2006 Bonds, and maturing on July 1 in each of the years 2007 through 2014, inclusive, all in accordance with the terms and conditions stated in the text of the Series 2006 Bonds.

WE HAVE EXAMINED the applicable and pertinent provisions of the Constitution and laws of the State of Texas and a transcript of certified proceedings of the City relating to the issuance of the Series 2006 Bonds, including (i) two ordinances of the City (the "*Master Ordinance Establishing the Airport System Revenue Bond Financing Program*" which was adopted by the City Council of the City on April 19, 2001, and the "*Eighth Supplement to the Master Ordinance*" which was adopted by the City Council of the City on November 16, 2006, which authorized the issuance of the Series 2006 Bonds (collectively, the "Ordinance"), (ii) the Escrow Agreement, dated as of November 1, 2006, between the City and The Bank of New York Trust Company, National Association, as Escrow Agent (the "Escrow Agreement"), (iii) the report and mathematical verifications of Grant Thornton LLP, certified public accountants, with respect to the adequacy of certain escrowed funds to accomplish the refunding purposes of the Bonds (the "Verification Report"), (iv) one of the executed Series 2006 Bonds (Bond No. T-1), and (v) the City's Federal Tax Certificate of even date herewith.

BASED ON SAID EXAMINATION, IT IS OUR OPINION that the Escrow Agreement has been duly authorized, executed and delivered by the City and constitutes a binding and enforceable agreement in accordance with its terms and that the "Refunded Bonds" (as defined in the Ordinance) being refunded by the Bonds are outstanding under the ordinance authorizing their issuance only for the purpose of receiving the funds provided by, and are secured solely by and payable solely from, the Escrow Agreement and the cash and investments, including the income therefrom, held by the Escrow Agent pursuant to the Escrow Agreement. In rendering this opinion, we have relied upon the verifications contained in the Verification Report as to the sufficiency of the cash and investments deposited pursuant to the Escrow Agreement for the purpose of paying the principal of, redemption premium, if any, and interest on the Refunded Bonds.

IT IS FURTHER OUR OPINION that the Series 2006 Bonds have been authorized, issued and delivered in accordance with law; that the Series 2006 Bonds constitute valid and legally binding special revenue obligations of the City in accordance with their terms (except as the enforceability thereof may be limited by bankruptcy, insolvency, reorganization, moratorium, liquidation and other similar laws now or hereafter enacted relating to creditors' rights generally); and that the Series 2006 Bonds, together with the outstanding "Parity Obligations" (as defined in the Ordinance), are payable from and secured by an irrevocable first lien on and pledge of the "Gross Revenues" of the City's "Airport System" (as such terms are defined in the Ordinance). The owners of the Series 2006 Bonds shall never have the right to demand payment of money raised or to be raised by taxation, or from any source whatsoever other than the Gross Revenues of the City's Airport System.

IT IS FURTHER OUR OPINION, except as discussed below, that the interest on the Series 2006 Bonds is excludable from the gross income of the owners for federal income tax purposes under the statutes, regulations, published rulings, and court decisions existing on the date of this opinion. The exceptions are as follows:

(1) interest on the Series 2006 Bonds will be includable in the gross income of the holder during any period that the Series 2006 Bonds are held by either a "substantial user" of the facilities refinanced with the proceeds of the Series 2006 Bonds or a "related person" of such user, as provided in section 147(a) of the Code; and

(2) interest on the Series 2006 Bonds will be included as an item of tax preference in determining the alternative minimum taxable income of the owner under section 57(a)(5) of the Code.

EXCEPT AS STATED ABOVE, we express no opinion as to any other federal, state, or local tax consequences of acquiring, carrying, owning, or disposing of the Series 2006 Bonds.

IN EXPRESSING THE AFOREMENTIONED OPINIONS as to the exclusion of interest from federal income taxes, we have relied on certain representations, the accuracy of which we have not independently verified, and assume compliance with certain covenants, regarding the use and investment of the proceeds of the Series 2006 Bonds and the use of the property refinanced therewith. We call your attention to the fact that if such representations are determined to be inaccurate or upon a failure by the City to comply with such covenants, interest on the Series 2006 Bonds may become includable in gross income retroactively to the date of issuance of the Series 2006 Bonds.

WE EXPRESS NO OPINION as to any insurance policies issued with respect to the payments due for the principal of and interest on the Series 2006 Bonds, nor as to any such insurance policies issued in the future.

THE CITY HAS RESERVED THE RIGHT, subject to the requirements stated in the Ordinance, to issue "Additional Parity Obligations" (as defined in the Ordinance) which also may be secured by and made payable from a first lien on and pledge of the aforesaid Gross Revenues of the City's Airport System on a parity with the Series 2006 Bonds and all other Parity Obligations then outstanding.

OUR SOLE ENGAGEMENT in connection with the issuance of the Series 2006 Bonds is as Bond Counsel for the City, and in that capacity, we have been engaged by the City for the sole purpose of rendering an opinion with respect to the legality and validity of the Series 2006 Bonds under the Constitution and laws of the State of Texas, and with respect to the exclusion from gross income of the interest on the Series 2006 Bonds for federal income tax purposes, and for no other reason or purpose. The foregoing opinions represent our legal judgment based upon a review of existing legal authorities that we deem relevant to render such opinions and are not a guarantee of a result. We have not been requested to investigate or verify, and have not independently investigated or verified, any records, data, or other material relating to the financial condition or capabilities of the City or the disclosure thereof in connection with the sale of the Series 2006 Bonds, and we have not assumed any responsibility with respect thereto. We express no opinion and make no comment with respect to the marketability of the Series 2006 Bonds and have relied solely on certificates executed by officials of the City as to the current outstanding Parity Obligations and as to the historical and projected Gross Revenues of the City's Airport System. Our role in connection with the City's Official Statement prepared for use in connection with the sale of the Series 2006 Bonds has been limited as described therein.

OUR OPINIONS ARE BASED ON EXISTING LAW, which is subject to change. Such opinions are further based on our knowledge of facts as of the date hereof. We assume no duty to update or supplement our opinions to reflect any facts or circumstances that may thereafter come to our attention or to reflect any changes in any law that may thereafter occur or become effective. Moreover, our opinions are not a guarantee of result and are not binding on the Internal Revenue Service (the "Service"); rather, such opinions represent our legal judgment based upon our review of existing law and in reliance upon the representations and covenants referenced above that we deem relevant to such opinions. The Service has an ongoing audit program to determine compliance with rules that relate to whether interest on state or local obligations is includable in gross income for federal income tax purposes. No assurance can be given whether or not the Service will commence an audit of the Series 2006 Bonds. If an audit is commenced, in accordance with its current published procedures the Service is likely to treat the City as the taxpayer. We observe that the City has covenanted not to take any action, or omit to take any action within its control, that if taken or omitted, respectively, may result in the treatment of interest on the Series 2006 Bonds as includable in gross income for federal income tax purposes.

Respectfully,

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APPENDIX F

SPECIMEN INSURANCE POLICY

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**FINANCIAL
SECURITY
ASSURANCE®**

MUNICIPAL BOND INSURANCE POLICY

ISSUER:

Policy No.: -N

BONDS:

Effective Date:

Premium: \$

FINANCIAL SECURITY ASSURANCE INC. ("Financial Security"), for consideration received, hereby UNCONDITIONALLY AND IRREVOCABLY agrees to pay to the trustee (the "Trustee") or paying agent (the "Paying Agent") (as set forth in the documentation providing for the issuance of and securing the Bonds) for the Bonds, for the benefit of the Owners or, at the election of Financial Security, directly to each Owner, subject only to the terms of this Policy (which includes each endorsement hereto), that portion of the principal of and interest on the Bonds that shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Issuer.

On the later of the day on which such principal and interest becomes Due for Payment or the Business Day next following the Business Day on which Financial Security shall have received Notice of Nonpayment, Financial Security will disburse to or for the benefit of each Owner of a Bond the face amount of principal of and interest on the Bond that is then Due for Payment but is then unpaid by reason of Nonpayment by the Issuer, but only upon receipt by Financial Security, in a form reasonably satisfactory to it, of (a) evidence of the Owner's right to receive payment of the principal or interest then Due for Payment and (b) evidence, including any appropriate instruments of assignment, that all of the Owner's rights with respect to payment of such principal or interest that is Due for Payment shall thereupon vest in Financial Security. A Notice of Nonpayment will be deemed received on a given Business Day if it is received prior to 1:00 p.m. (New York time) on such Business Day; otherwise, it will be deemed received on the next Business Day. If any Notice of Nonpayment received by Financial Security is incomplete, it shall be deemed not to have been received by Financial Security for purposes of the preceding sentence and Financial Security shall promptly so advise the Trustee, Paying Agent or Owner, as appropriate, who may submit an amended Notice of Nonpayment. Upon disbursement in respect of a Bond, Financial Security shall become the owner of the Bond, any appurtenant coupon to the Bond or right to receipt of payment of principal of or interest on the Bond and shall be fully subrogated to the rights of the Owner, including the Owner's right to receive payments under the Bond, to the extent of any payment by Financial Security hereunder. Payment by Financial Security to the Trustee or Paying Agent for the benefit of the Owners shall, to the extent thereof, discharge the obligation of Financial Security under this Policy.

Except to the extent expressly modified by an endorsement hereto, the following terms shall have the meanings specified for all purposes of this Policy. "Business Day" means any day other than (a) a Saturday or Sunday or (b) a day on which banking institutions in the State of New York or the Insurer's Fiscal Agent are authorized or required by law or executive order to remain closed. "Due for Payment" means (a) when referring to the principal of a Bond, payable on the stated maturity date thereof or the date on which the same shall have been duly called for mandatory sinking fund redemption and does not refer to any earlier date on which payment is due by reason of call for redemption (other than by mandatory sinking fund redemption), acceleration or other advancement of maturity unless Financial Security shall elect, in its sole discretion, to pay such principal due upon such acceleration together with any accrued interest to the date of acceleration and (b) when referring to interest on a Bond, payable on the stated date for payment of interest. "Nonpayment" means, in respect of a Bond, the failure of the Issuer to have provided sufficient funds to the Trustee or, if there is no Trustee, to the Paying Agent for payment in full of all principal and interest that is Due for Payment on such Bond. "Nonpayment" shall also include, in respect of a Bond, any payment of principal or interest that is Due for Payment

made to an Owner by or on behalf of the Issuer which has been recovered from such Owner pursuant to the United States Bankruptcy Code by a trustee in bankruptcy in accordance with a final, nonappealable order of a court having competent jurisdiction. "Notice" means telephonic or telecopied notice, subsequently confirmed in a signed writing, or written notice by registered or certified mail, from an Owner, the Trustee or the Paying Agent to Financial Security which notice shall specify (a) the person or entity making the claim, (b) the Policy Number, (c) the claimed amount and (d) the date such claimed amount became Due for Payment. "Owner" means, in respect of a Bond, the person or entity who, at the time of Nonpayment, is entitled under the terms of such Bond to payment thereof, except that "Owner" shall not include the Issuer or any person or entity whose direct or indirect obligation constitutes the underlying security for the Bonds.

Financial Security may appoint a fiscal agent (the "Insurer's Fiscal Agent") for purposes of this Policy by giving written notice to the Trustee and the Paying Agent specifying the name and notice address of the Insurer's Fiscal Agent. From and after the date of receipt of such notice by the Trustee and the Paying Agent, (a) copies of all notices required to be delivered to Financial Security pursuant to this Policy shall be simultaneously delivered to the Insurer's Fiscal Agent and to Financial Security and shall not be deemed received until received by both and (b) all payments required to be made by Financial Security under this Policy may be made directly by Financial Security or by the Insurer's Fiscal Agent on behalf of Financial Security. The Insurer's Fiscal Agent is the agent of Financial Security only and the Insurer's Fiscal Agent shall in no event be liable to any Owner for any act of the Insurer's Fiscal Agent or any failure of Financial Security to deposit or cause to be deposited sufficient funds to make payments due under this Policy.

To the fullest extent permitted by applicable law, Financial Security agrees not to assert, and hereby waives, only for the benefit of each Owner, all rights (whether by counterclaim, setoff or otherwise) and defenses (including without limitation, the defense of fraud), whether acquired by subrogation, assignment or otherwise, to the extent that such rights and defenses may be available to Financial Security to avoid payment of its obligations under this Policy in accordance with the express provisions of this Policy.

This Policy sets forth in full the undertaking of Financial Security, and shall not be modified, altered or affected by any other agreement or instrument, including any modification or amendment thereto. Except to the extent expressly modified by an endorsement hereto, (a) any premium paid in respect of this Policy is nonrefundable for any reason whatsoever, including payment, or provision being made for payment, of the Bonds prior to maturity and (b) this Policy may not be canceled or revoked. THIS POLICY IS NOT COVERED BY THE PROPERTY/CASUALTY INSURANCE SECURITY FUND SPECIFIED IN ARTICLE 76 OF THE NEW YORK INSURANCE LAW.

In witness whereof, FINANCIAL SECURITY ASSURANCE INC. has caused this Policy to be executed on its behalf by its Authorized Officer.

[Countersignature]

FINANCIAL SECURITY ASSURANCE INC.

By _____

By _____

Authorized Officer

A subsidiary of Financial Security Assurance Holdings Ltd.
31 West 52nd Street, New York, N.Y. 10019

(212) 826-0100

Form 500NY (5/90)